

## Deal Terms

1 SAVE = \$33.5 (incl. \$2.50 prepayment) +  
ticking fee of \$0.10/month

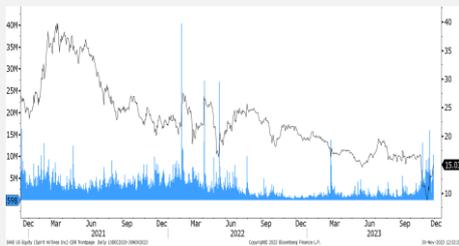
### Target: Spirit Airlines

Country	US
Bloomberg	SAVE
Sector	Airlines
Share price (USD)	14.29
Market cap (USD mn)	1,560
Free float %	~99

### Acquirer: JetBlue

Country	US
Bloomberg	JBLU
Sector	Airlines
Share price (USD)	4.37
Market cap (USD mn)	1,456
Free float	~99

### JBLU Price Chart



Deal status: Trial to end in December 2023

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## Spirit Airlines (SAVE) / JetBlue Airways (JBLU) Update

We still believe that the DOJ has the upper hand as the acquisition will eliminate ULCC competition in most routes SAVE services today and possible harms appear to outweigh deal benefits.

### CBR view:

- The DOJ complaint echoes our concerns articulated in our [report](#) dated July 22, 2022.
- While JBLU and American have unwinded their Northeast Alliance to help their case and have offered divestitures, we still believe that the DOJ is likely to prevail.
- Each of SAVE and JBLU sees the other as a close competitor.
- JBLU argues that customers will benefit from the merger due to the “JetBlue effect”, which has forced the big4 to reduce prices.
- We accept that JBLU’s presence in a market leads to lower prices, however that is true for the higher end of the market as both the big4 and JBLU offer a broader range of services as compared to ultra low cost carriers (ULCCs).
- The key obstacle, in our view, is that competition in the ULC segment will be lost in all routes where SAVE is present today except for to-be-divested city pairs.
- SAVE is the largest ULCC and most of these routes will be left with no or with limited ULCC competition, therefore will most likely result in increased prices in this segment.
- As per industry experts, the ULC segment has different characteristics as demand is very price sensitive. If no ULCC option is left, customers are likely to forego air travel.
- The merging parties might argue that merger benefits in the upper segment outweigh harms, however we are sceptical of that.
- The DOJ estimates that the loss of Spirit’s ULC model will lead to a net loss of \$1b per annum. JBLU claims to have saved customers \$10b since its launch.
- Assuming that most of these savings can be attributed to the past 10-15 years means \$0.66-\$1b annual savings at an average 4-5% market share.
- SAVE – after divestitures – might add 3.5-4% to JBLU’s market share, so around an additional \$0.46 – \$0.88b annual savings resulting from the JBLU effect.
- Based on the above, if we accept the DOJ’s and JBLU’s estimates, harms resulting from the merger outweigh deal benefits.
- Also, the DOJ might care more about the loss of competition between SAVE and JBLU and the loss of ULCC option in most of SAVE’s markets than the balance of benefits and harms that materialize in different market segments.
- The DOJ also claims that risk of coordination will increase with the loss of SAVE.

### Timing

- The trial is expected to end on December 5, with a ruling seen in late-December or early next year.
- The Outside Date is January 28, 2024, which might be extended to July 24, 2024.
- In case the companies lose, JBLU has to appeal. If they win, a timely DoT approval might prove problematic as the agency has articulated its opposition to the merger.

### Downside

- Both Frontier and JetBlue are down ~70% since Jan 2022 and ALGT has lost 63% in that period.
- Based on peers’ performance, SAVE could be down to cca\$6/share in case the deal breaks.

## Key risks

### REGULATORY APPROVALS / TIMING

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#### Key points of the DOJ complaint:

- **Each of SAVE and JBLU sees the other as a close competitor:**
  - The merger would eliminate vigorous head-to-head competition between JetBlue and Spirit that benefits cost-conscious travelers on hundreds of routes today.
  - JetBlue has recognized that its own fares and revenues on a route drop significantly when Spirit enters.
  - Before the end of 2023, Spirit independently expected to add service in five new cities and increase daily departures from Fort Lauderdale, Orlando, and Los Angeles—all JetBlue focus cities. And over the next five years Spirit plans to add nonstop service to several routes JetBlue flies today. The acquisition stops this future competition before it starts
  - **In 2022, JetBlue concluded that when Spirit exits a route, fares increase by 30% on average.**
    - Spirit had previously estimated in years prior to 2018 that its prices to destinations it serviced were on average 30% lower than other airlines.
  - JetBlue created a “Spirit Competitive Strategy” with the goal of developing an “integrated strategy to better compete with Spirit,” which JetBlue’s Head of Revenue and Planning viewed as “critical.”
  - Spirit similarly views JetBlue as a close competitor. In 2019, after JetBlue initiated a sale across hundreds of routes in its network, Spirit responded by lowering its fares for multiple routes where the two carriers competed head-to-head
  - Spirit’s Board of Directors recognized the antitrust and regulatory risks of mergers in an already consolidated airline industry, and recommended that Spirit shareholders vote to adopt the merger agreement with Frontier instead, concluding that “consummation of the proposed JetBlue combination, with the [Northeast Alliance] remaining in place, seemed almost inconceivable.” “Even putting aside the Northeast Alliance,” Spirit warned that JetBlue’s stated plans to reconfigure Spirit’s planes would “significantly diminish[] capacity” and “result in higher prices for consumers.” Accordingly, “a court . . . will be very concerned that a **JetBlue-Spirit combination will result in a higher-cost/higher fare airline that would eliminate a lower cost/lower fare airline and remove about half of the [ultra-low-cost] capacity in the United States.**”
- **The net harm to consumers from eliminating Spirit as a competitor, DOJ projected, would be roughly \$1 billion annually.**
  - The Elimination of Spirit’s Business Model Would Harm Cost-Conscious Customers in Particular
  - JetBlue’s acquisition of Spirit would deprive cost-conscious customers of the option to choose Spirit and its low-priced, unbundled fares wherever Spirit flies today or wherever Spirit’s growth plans would have it fly in the near future.
  - **Harm to these cost-conscious travelers would also occur on routes where Spirit competes against other carriers and JetBlue is absent today.**
  - **JetBlue has been consistent about its plans for the combined company; it plans to retrofit existing Spirit aircraft to match JetBlue configurations, thereby eliminating 10 to 15% of the capacity**—approximately 20 to 28 seats— from each plane. Further, in justifying the deal internally and to the company’s lenders, **JetBlue predicted that it would reap 24% more revenues per seat than Spirit earns today**, on the assumption that “customers see value of [the] better product and experience[,] and are glad to adjust.”
- **Risk of coordination among remaining airlines increases with the loss of Spirit.**
  - The airline industry is vulnerable to coordination. JetBlue has demonstrated a willingness to engage in such coordinated behavior.
  - Large airlines often “lead” ticket prices by briefly lowering air ticket costs for a particular flight to see if other airlines follow suit, and then raising the price again if they do not.
  - Based on historical evidence, SAVE was not a follower in terms of pricing.
    - Spirit does not typically match JetBlue’s price increases, nor does it often use ATPCO to lead fare increases.
  - In response to increased competition from Spirit and its use of unbundled fares, the three largest airlines in the country—Delta, United, and American Airlines—introduced their “basic economy” fares in 2012, 2016, and 2017 respectively, which offered customers more choice and control over how they spent their money.
- **JBLU / American alliance (has been unwound since)**
  - Both JetBlue and American Airlines admit that, on these routes—which account for 75 percent of JetBlue’s total capacity—they coordinate and do not compete.
  - The acquisition also would reduce competition on routes outside the scope of the Northeast Alliance where Spirit and American Airlines both offer nonstop service today.
    - JetBlue is less likely than Spirit to compete aggressively with American Airlines going forward

**SAVE/JBLU arguments:****■ Financial difficulties:**

- Spirit Airlines Inc.'s top executive told a judge that the low-cost carrier suffered years of pandemic-fueled losses that show no signs of ending, which pushed the company into a merger with JetBlue Airways Corp.
- **CBR Comment:** Courts have not endorsed the failing firm defense in past merger cases, especially when alternative bidders were present.
  - The failing firm defense is a high bar to meet. In addition to the financial standards, **a company will have to show that it conducted an exhaustive search for alternative buyers that proves none exist.** Moreover, provisions in a transaction agreement that limit the ability of the failing firm seek or consider competing offers may be harmful to failing firm arguments.

**■ Increased competition:**

- The proposed acquisition of Spirit would turbocharge JetBlue's growth, create the first nationwide competitor to the Big Four, and result in billions of dollars of savings for the traveling public.
  - "You'd never, ever get to the size they are based on organic growth,"
- Low-cost service has its limits. There are simply not enough passengers in the market who make their travel decisions solely based on price.
  - "The government says that but for this deal Spirit will continue to grow as fast or faster than it did in the past," Spirit attorney Jay Cohen said. "The reality is that Spirit's financial performance will not permit the growth that Spirit planned for."
- The void will be filled by other low cost airlines.
  - Plaintiffs' purported concern about the loss of a ULCC like Spirit, and how that might impact cost-conscious travelers, ignores that JetBlue and other airlines will continue to offer unbundled fares and that the ULLC model will continue to be available for the smaller segment of the flying public that wants it.
  - In the last few years, ULCCs including Frontier, Allegiant, and Sun Country have all either grown significantly or announced plans for expansion. Two new ULCCs, Avelo and Breeze, launched and dramatically expanded their service
  - CBR comment: The DOJ is skeptical given the shortage of planes, pilots, slots.
- **United aims to compete for low cost fliers aggressively** as it expands its fleet with bigger aircraft capable of offering more seats for its bare bones basic economy offering.

**■ Divestitures**

- **JetBlue offered to divest gates and landing and takeoff rights and gates in Boston, the New York City area and Fort Lauderdale, Florida, to Frontier and Allegiant.**
  - JetBlue will shift all of Spirit's holdings at Boston Logan International and Newark Liberty International and part of its assets at Fort Lauderdale-Hollywood International in Florida to Allegiant Travel Co.
  - Under the agreement, JetBlue will transfer to Allegiant two gates in Boston and two gates in Newark, along with the rights for 43 takeoff and landing slots at Newark. JetBlue also will give up five gates at Fort Lauderdale to the Broward County Aviation Department and will work with the agency on Allegiant's use of the gates.
  - JetBlue previously agreed to divest Spirit's holdings at New York's LaGuardia Airport to deep discounter Frontier Group Holdings Inc.
- The divestitures are subject to approval by local airport authorities, the Federal Aviation Administration and the US Transportation Department and will only occur after the JetBlue-Spirit transaction closes. Similar terms govern the Frontier agreement.

**■ The "JetBlue Effect"**

- Legacy airlines have to offer lower prices in markets where JBLU is present
- The JetBlue Effect was first noted in an MIT study
  - In 2012, the presence of JetBlue Airways, another low-cost carrier, was associated with a decrease of about \$32 in average one-way fare, controlling for average itinerary distance and other low-cost carrier competition.
- Today, JetBlue has less than a 5% share of airline seats in the United States combination with Spirit would give JetBlue approximately a 9% share of airline seats.
- That will mean **billions of dollars more in consumer savings** only "overlap" on about 11% of the nonstop routes that both airlines fly.

**■ The ULC segment: ([source](#))**

- Low-cost and legacy airlines are very different types of airlines, and the budget airlines appeal to a very different type of customer," says Henry Hartevelde, a travel industry and airline analyst.
- The mere presence of a low-cost carrier benefits everybody, as it forces the majors to lower their fares.
  - The September Consumer Price Index report from the US Bureau of Labor Statistics (BLS) shows the average airline fare across carriers has fallen 13% year-over-year.
- **Low-cost carriers fill "a necessary gap" in the market: if those carriers didn't exist, there likely wouldn't be any other airlines to service low-income flyers.**

- If travellers were faced with the choice between paying more to fly on a full-service airline or simply not traveling at most people would choose to stay home.
  - Even if there are only a relative handful of low-cost carriers, they serve as a buoy to keep airfares from increasing.
    - "The mere presence of a low-cost carrier benefits everybody as it forces the majors to lower their fares." If those airlines do go away – as Spirit might if it does merge with JetBlue – "people will be paying more in every city and every route."

#### Department of Transportation approval:

- The Department has the authority to effectively block airline mergers that would stifle competition.
  - Under 49 U.S.C. § 41102, airlines must receive a certificate from the Department that authorizes them to operate (whether domestically or internationally).<sup>18</sup> The Secretary of Transportation must grant these airlines the “economic authority” to operate and must approve any transfer of operating certificates to another carrier, authority that gives the Secretary de facto merger-blocking power.
  - **Certificate transfers are only permitted when the Secretary determines that a transfer would be “consistent with the public interest.”** If a transfer is approved, the Secretary must include a report that discusses the effects of the transfer on, among other areas, “competition in the domestic airline industry.” Airlines can be exempted from these requirements, but this exemption must also be “consistent with the public interest.”
  - The Department has already promulgated regulations under these authorities specifying that it can suspend or revoke certain air carrier authorizations upon a determination that it is “in the public interest to do so.”
- DOT [statement](#) on lawsuit:
  - In light of the Justice Department’s pending litigation, **USDOT plans to deny the exemption application.** The Department will continue to separately **investigate the transfer as part of its statutory public interest mandate** and under its authority to enforce against unfair and deceptive practices and unfair methods of competition. **The investigation will remain open for the duration of the proceeding.**
    - The DoT’s Buttigieg clarified that he could not comment much on the JetBlue-Spirit merger due to the trial, but said the DOT supports the Department of Justice's view on the merger.
  - **BBG: If the DOT decides the certificate transfer is not in the public’s interest, the companies would have to sue the agency** successfully if they want to consummate the deal, said William Kovacic, a former Federal Trade Commission chairman.
    - The DOT said its investigation would remain open “for the duration” of the Justice Department lawsuit challenging the merger under the Clayton Act. That potentially complicates the companies’ effort to close their deal by July 2024, as outlined in their merger agreement.

#### The Northeast Alliance

- In July 2020, JetBlue and American entered into the NEA designed to optimize our respective networks at JFK, LaGuardia, Newark, and Boston. Following review and agreement by the DOT, JetBlue and American began implementing the NEA in July 2021. On September 21, 2021, the United States Department of Justice, along with the Attorneys General of six states and the district of Columbia filed suit against JetBlue and American seeking to enjoin the NEA, alleging that it violates Section 1 of the Sherman Act.
- The Northeast Alliance combines American’s and JetBlue’s operations at four major airports: Boston Logan, John F. Kennedy, LaGuardia and Newark Liberty. The airlines have committed to coordinate “on all aspects” of network planning, including which routes to fly, when to fly them, who will fly them and what size planes to use for each flight. The two airlines planned to share revenues earned at these airports, eliminating their incentives to compete with one another. The Northeast Alliance will also allow the parties to pool their gates and takeoff and landing authorizations, known as “slots.”
- **U.S. District Judge Leo Sorokin ruled in May the airlines' "Northeast Alliance" that allowed the two carriers to coordinate flights and pool revenue violated antitrust law.**
  - In its May 19 Opinion, the court analyzed the NEA using the rule of reason and concluded that it violated Section 1 of the Sherman Act. To begin, the court held that the DOJ had proven that the NEA has already caused actual harm to competition. Specifically, the court found that the NEA “eliminated the once vigorous competition between two of the four largest domestic carriers in the northeast, replacing it with broad cooperation in pursuit of the shared interests of the partnership.”
  - The court also determined that through the NEA, JetBlue had weakened its status as a “maverick” in the industry. Moreover, the court explained that JetBlue and American’s assignment of routes between themselves was a “straightforward example of market allocation” that “closely resembles a restraint that is per se illegal.
  - The court also found that JetBlue and American had not produced substantial evidence of the procompetitive benefits they claim arise from the NEA, including the creation of a larger NEA network with better connectivity, as well as the creation of better schedules by allocating various routes between themselves. In fact, the court held that the “overarching purpose of the NEA is anticompetitive
- **As of July 21, 2023 codeshare flights between American and JetBlue will no longer be available for sale** and you will no longer be able to redeem miles for flight awards on JetBlue. Existing flight award reservations will be honored but changes will not be allowed.
- **American Airlines appeals court ruling halting JetBlue alliance**
  - JetBlue previously said it would not appeal as it seeks to protect a planned \$3.8 billion purchase of Spirit Airlines that faces a separate legal challenge from the Justice Department.

**Timing:**

- The trial is expected to end on December 5.
- **A ruling is expected late December or early next year.**
- We note that as per the DMA, JBLU has to appeal if they lose in court.
  - “The Merger Agreement also contains certain provisions relating to efforts to obtain regulatory approval of the Merger, including to provide that JetBlue and Spirit, in connection with obtaining any necessary approval of a governmental entity (including under the HSR Act), will use their respective reasonable best efforts to take, or cause to be taken, all appropriate actions to obtain such approvals, including to **contest, defend and appeal any proceeding brought by a governmental entity challenging or seeking to prohibit the consummation of the Merger**, provided that JetBlue shall not be required to take any divestiture actions if such action would or would reasonably be expected to result in a material adverse effect on JetBlue and its subsidiaries (including Spirit and its subsidiaries) after giving effect to the transactions contemplated by the Merger Agreement, taken as a whole, and in no event shall JetBlue be required to agree to any such divestiture action that, in JetBlue’s discretion, would be reasonably likely to materially and adversely affect the anticipated benefits of the parties to the Northeast Alliance Agreement between JetBlue and American Airlines, Inc., dated as of July 15, 2020, and the agreements contemplated thereby. Any such divestiture action may be conditioned upon the closing of the Merger.”
- JBLU says it still expects to close the Spirit transaction in the first half of 2024.
- The Outside Date is January 28, 2024, which might be extended to July 24, 2024.

**CBR view:**

- **The DOJ complaint echoes our concerns articulated in our [report](#) dated July 22, 2022.**
- **While JBLU and American have unwinded their Northeast Alliance to help their case, we still believe that the DOJ is likely to prevail.**
- **JBLU argues that customers will benefit from the merger due to the “JetBlue effect”, which has forced the big4 to reduce prices and according to JBLU’s estimate has saved customers \$10bn since its launch.**
- **We accept that JBLU’s presence in a market leads to lower prices, however that is true for the higher end of the market as both the big4 and JBLU offer a broader range of services as compared to ultra low cost carriers (ULCCs).**
- **The key obstacle in our view is that competition in the ULC segment will be lost in all routes where SAVE is present today except for to-be-divested city pairs.**
- **SAVE is the largest ULCC provider and most of these routes will be left with no, or with limited ULCC competition, therefore will most likely result in increased prices in this segment.**
- **As per industry experts, the ULC segment has different characteristics as demand is very price sensitive. If no ULCC option is left, customers are likely to forego air travel.**
- **The merging parties might argue that merger benefits in the upper segment outweigh harms, however we are sceptical of that.**
  - **The DOJ estimates that the loss of Spirit’s ULC model will lead to a net loss of \$1b per annum.**
  - **JetBlue’s own internal estimates show that it has saved customers at least \$10 billion since its launch, offering lower fares and better service and forcing its competitors to do the same.**
  - **Assuming that most of these savings can be attributed to the past 10-15 years means \$0.66-\$1b annual savings at an average 4-5% market share.**
  - **SAVE – after divestitures – might add 3.5-4% to JBLU’s market share, so around an additional \$0.46 – \$0.88b annual savings resulting from the JBLU effect.**
- **Based on the above, if we accept the DOJ’s and JBLU’s estimates, harms resulting from the merger outweigh deal benefits.**
- **Also, the DOJ might care more about the loss of competition between SAVE and JBLU and the loss of ULCC option in most of SAVE’s markets than the balance of benefits and harms that materialize in different market segments.**

**JBLU COMMITMENT / POSSIBLE PRICE CUT**

- Wall Street analysts are increasingly calling for it to lower the purchase price given all of Spirit’s problems.
- SAVE financial health:
  - JetBlue and Spirit are expected to lose money again next year, and maybe in 2025.
  - One big issue is the grounding of many Airbus A320neo-family aircraft powered by Pratt & Whitney geared turbofan engines. Both airlines are affected but the situation is more pronounced at Spirit, which anticipates having an average of 26 aircraft grounded at any given time next year. The number is forecast to peak at 41 aircraft in December.
  - Spirit only operates 202 aircraft, of which 88 are A320neo-family aircraft with Pratt engines.
- We note that industry-wide effects are carved out of the MAE definition, thus we believe that the grounding of Airbus aircraft and the weakness of the whole ULCC segment does not enable JBLU to trigger a MAE.
- MAE definition:
  - “Company Material Adverse Effect” means any change, event, circumstance, development, condition, occurrence or effect that (a) has had, or would reasonably be expected to have, individually or in the aggregate, a material adverse effect on the

business, financial condition, assets, liabilities or results of operations of the Company Group, taken as a whole, or (b) prevents, or materially delays, the ability of the Company to consummate the transactions contemplated by this Agreement; provided, however, that none of the following will be deemed in themselves, either alone or in combination, to constitute, and that none of the following will be taken into account in determining whether there has been or will be, a Company Material Adverse Effect: (i) any development in general economic conditions, or in securities, credit or financial markets, including changes in interest rates and changes in exchange rates, in the United States or any other country or region in the world in which the Company conducts business or **any industry-wide development generally affecting airline companies**; (ii) any change in GAAP or any change in applicable Laws applicable to the operation of the business of the Company; (iii) any change resulting from the announcement or pendency of the transactions contemplated by this Agreement, including the Merger (it being understood that this clause (iii) shall not apply to any representation, warranty, covenant or agreement of the Company herein that is expressly intended to address the consequences of the execution, delivery or performance of this Agreement or the consummation of the transactions contemplated hereby); (iv) acts of war, outbreak or escalation of hostilities, terrorism or sabotage, or other changes in geopolitical conditions, earthquakes, hurricanes, tsunamis, tornados, floods, mudslides, wild fires or other natural disasters, any epidemic, pandemic, outbreak of illness or other public health event (including, for the avoidance of doubt, COVID-19 and impact of COVID-19 on the Company) and other similar events in the United States or any other country or region in the world in which the Company conducts business; (v) any failure by the Company to meet any internal or published (including analyst) projections, expectations, forecasts or predictions in respect of the Company's revenue, earnings or other financial performance or results of operations (it being understood that the underlying facts and circumstances giving rise to such event may be deemed to constitute, and may be taken into consideration in determining whether there has been, a Company Material Adverse Effect); (vi) the taking of any action expressly contemplated by this Agreement or at Parent's or Merger Sub's request; or (vii) any change in the market price or trading volume, or the downgrade in rating, of the Company's securities (it being understood that the underlying facts and circumstances giving rise to such event may be deemed to constitute, and may be taken into consideration into determining whether there has been, a Company Material Adverse Effect); provided, further, that the effects or changes set forth in the foregoing clauses (i), (ii) and (iv) shall be taken into account in determining whether there has occurred a Company Material Adverse Effect only to the extent such developments have, **individually or in the aggregate, a disproportionate impact on the Company relative to other companies in the airline industry**, in which case only the incremental disproportionate impact may be taken into account.

## Valuation

### DOWNSIDE

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- Both Frontier and JetBlue are down ~70% since Jan 2022 and ALGT has lost 63% in that period.
- Based on peers' performance, SAVE could be down to cca\$6/share in case the deal breaks.

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**Disclosures:**

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