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M&A Outlook Rocky Following Trump Victory

By **Chelsea Naso**

Law360, New York (November 9, 2016, 6:32 PM EST) -- President-elect Donald Trump's surprise win may have only temporarily sent the stock market reeling, but the ongoing uncertainty surrounding his planned changes to a broad array of regulations and policies could prove challenging for U.S.-targeted deal-making, experts say.

As Trump gained ground Tuesday evening, stock futures plummeted amid concerns that the election would not turn out as predicted. Overnight, Trump secured his role as president-elect, confirming the uncertainty felt by the markets. By the end of trading on Wednesday, however, the stock market had sparked a drastic turnaround, with the Dow Industrial Average, the Nasdaq Composite and the S&P 500 all posting gains as of the closing bell.

“After an election that’s so unexpected, there is going to be uncertainty. It’s an obvious point, but it’s an important point,” Simpson Thacher & Bartlett LLP corporate partner Mark Pflug said. “People can say, ‘Well the markets are stable and flat this morning.’ But just last night, they were down 800 points, which proves the point that nobody really knows.”

Although the U.S. markets were only down briefly, the uncertainty will likely persist until it becomes more clear which campaign promises Trump plans to make good on, Pflug noted.

“For the next six months or so — maybe a little less, maybe a little more — there’s going to be a fair amount of uncertainty associated with the transition and some of the early stage decisions that he has stated publicly that he desires to make,” he said.

Uncertainty in the stock market, as well as over potential regulatory changes, is likely to weigh on mergers and acquisitions until Trump’s administration and until plans begin to take shape and buyers and sellers have the opportunity to digest what the changes will mean for them.

“In the short run, there is uncertainty, and uncertainty is always bad for the stock markets and for M&A. People will need to take a pause and address what the election of Donald Trump and what the policies he has said he will pursue means,” said Robert Townsend, co-chair of Morrison & Foerster LLP’s global M&A practice group.

With worries about antitrust enforcement, tax code changes, modifications to trade and immigration policies potentially in the works, it can be difficult for companies or investment funds to lock down an appropriate valuation for a target.

“I just think all of this uncertainty really just takes the air out of the room for a board or for an investment firm when they are evaluating a potential target company. They don’t know what to expect in these matters, and that affects their ability to pull the trigger in terms of valuation,” said Howard Spilko, co-chair of Kramer Levin Naftalis & Frankel LLP’s corporate department.

That will send the M&A market into a wait-and-see mode, a stark contrast to the record-high activity recorded in the U.S. in October, when U.S.-targeted M&A rose to $356.8 billion in deal value, according to Dealogic. That eclipsed the previous monthly high of $332.3 billion in deals announced in July 2015.

Even so, there's a strong chance that the lull will not persist. Once Trump’s plans become clear, it's expected that most deal makers will pick up where they left off, explained David Shine, chair of Paul Hastings LLP's New York M&A practice. The economic factors driving M&A are likely to still be there. Companies and private equity firms are sitting on a lot of capital that needs to be invested, and there is still a push for inorganic growth.

“The conventional wisdom is that M&A doesn’t like uncertainty. And if there’s one sensitivity that surrounds Trump, it’s uncertainty. ... So in the short term, M&A deals are going to face some choppy waters. My guess is that there is going to be a little bit of a lull,” Shine said.

“But I also think that once the markets get their land legs back, M&A is going to have a lot of opportunity,” he added.

One potential area for opportunity is in antitrust regulation, which may see a more relaxed approach. Trump’s administration will be tasked with filling some open seats at the Federal Trade Commission and the U.S. Department of Justice, suggesting that a more traditional Republican viewpoint may take hold.

“There are vacancies at the FTC and the Department of Justice, and they are now going to be filled by a Republican president and a Republican senate. And those seats, when filled by Republicans, have traditionally been filled with people who are more deal-friendly,” Shine said.

Trump, however, is not a traditional Republican. He has pledged to block the tie-up of AT&T Inc. and Time Warner Inc., as well as come down hard on transactions that may harm the very constituents that lifted him into office, breeding uncertainty about how his administration will deal with M&A.

“There will be perhaps a looser enforcement of antitrust rules and M&A at a general level, but at the same time, because of the populist positioning of Donald Trump, there will be a need and desire to aggressively take on very high-profile transactions that are seen as undermining competition or not in the best interest of American consumers or Midwestern workers,” Townsend said.

The president-elect’s tax proposals do, on the other hand, fall more in line with traditional Republican values. His proposals on the campaign trail borrowed largely from the House Republicans’ blueprint for tax reform, which purports to simplify the tax code and encourage investment by eliminating deductions and estate taxes and cutting individual and business tax rates.

Trump has also called for taxing income that flows to individual owners of pass-through entities at his proposed 15 percent corporate rate, rather than at the individual rate at which it's currently taxed. His 15 percent corporate rate will "unleash new job creation," prevent corporate inversions and "cause trillions in new dollars and wealth to come pouring into our country," he has said.

Those tax proposals would have varying effects on the M&A market. Cutting individual and business taxes may open up more money for acquisitions or investments in general, according to Dykema Gossett PLLC's annual M&A outlook survey, which was released earlier this month.

"Our respondents felt really strongly that a decrease in corporate taxes and personal income taxes would have a positive impact on the U.S. M&A market," said Dykema corporate member Thomas Vaughn. "I think most of us expected gridlock. But with a totally controlled Congress and executive office, we could see tax change. If you believe that's positive for M&A, which our respondents do, that could actually be good for M&A here."

At the same time, the proposed changes to carried interest may prove challenging for the private equity industry, explained Baker Botts LLP's Samantha Crispin.

"This change would have a significant impact on the compensation earned by private equity and hedge fund managers and venture capitalists and could lead to changes in investment strategies and potentially fewer investments in start-up and distressed U.S. companies," she said via email.

Deal makers may also be affected by Trump's plans to repeal much of President Barack Obama's changes, such as the Affordable Care Act, along with his commentary on foreign investment in the U.S., his promises to take a tough stance on immigration and his plans to renegotiate major trade deals.

"In the longer run, if Trump does pursue the policies he has articulated so far, the change in our trade policy, the change in our defensive relationships with our traditional allies, the change in tax policy in the U.S., that will further ongoing uncertainty and will likely have the effect of diminishing cross-border trade and will likely have a negative impact on a number of U.S. companies that are major exporters and could make the U.S. a less attractive place for inbound investment," Townsend said.

"Historically, we have been the most attractive place in the world for foreign capital to come in and invest and support our growth. I think it will have a negative effect on cross-border transaction," he added.

--Editing by Christine Chun.