M&A INSIGHTS:

ELECTION CYCLES AND THE IMPACT ON M&A ACTIVITY

WRITTEN BY JUSTIN PINTO, VICE PRESIDENT, CHARTER CAPITAL

OCT 2024

CHARTER CAPITAL • 140 Monroe Center NW, Suite 300 • Grand Rapids, MI • chartercapitalpartners.com • 616.235.3555

M&A INSIGHTS

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Introduction

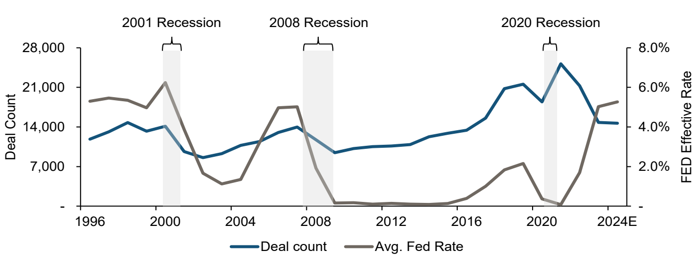
Mergers and acquisitions ("M&A") are essential tools for corporate growth, enabling companies to expand market share, diversify portfolios, and achieve economies of scale. Yet, M&A activity is significantly influenced by external factors such as political election cycles, and macroeconomic conditions. As the 2024 presidential election approaches, speculation about its potential impact on M&A activity has intensified, especially for lower middle-market businesses considering a sale.

This whitepaper explores how election cycles can influence deal volumes, valuations, and overall market dynamics, drawing on insights from historical data and current trends. While political uncertainty can pose challenges, our analysis suggests that the overall impact on M&A activity is often less severe than anticipated. By understanding the key factors at play, business owners can make informed decisions and effectively position their businesses for success amid the complexities of the M&A landscape during election years.

Historical M&A Activity and Economic Health

Election cycles often introduce uncertainty for those considering an M&A strategy, as policy shifts following an election can impact market conditions. This can contribute to market volatility, particularly affecting the timing of M&A activity. Charter's analysis of U.S. M&A deal volumes since 1996 shows that post-election year volumes tend to decline by approximately 8.0% to 10.0% compared to the previous year. However, this dip often reflects only a delay, with many deals re-entering the market shortly thereafter. Our findings indicate that M&A activity during election years is largely influenced by broader macroeconomic cycles rather than by the election cycle itself as seen in the M&A transaction announcement chart below.

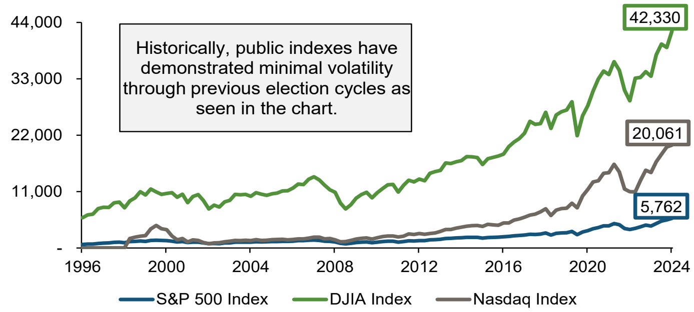
M&A Transaction Announcements[1]



1. Source: IMAA-Institute and FRED. Data includes U.S. M&A transactions. 2024 is annualized.

Our analysis also included a review of key macroeconomic indicators such as the S&P 500, Dow Jones Industrial Average, and NASDAQ to examine how economic health correlates with M&A activity during election cycles. The results indicate a positive correlation which shows the stability and resilience of the broader economy tend to boost confidence among both buyers and sellers driving M&A transactions. Any M&A slowdown that occurs during election years is typically temporary, with activity rebounding shortly after the election period concludes.

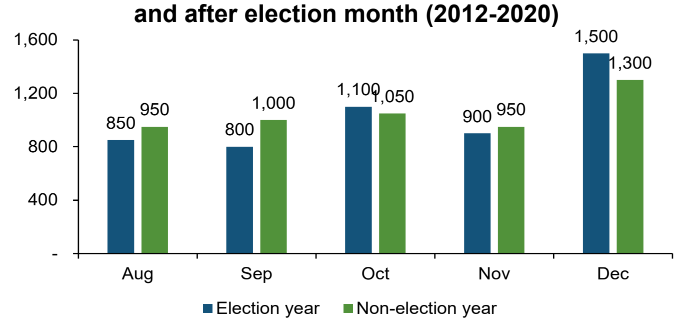
Quarterly Public Index[1]

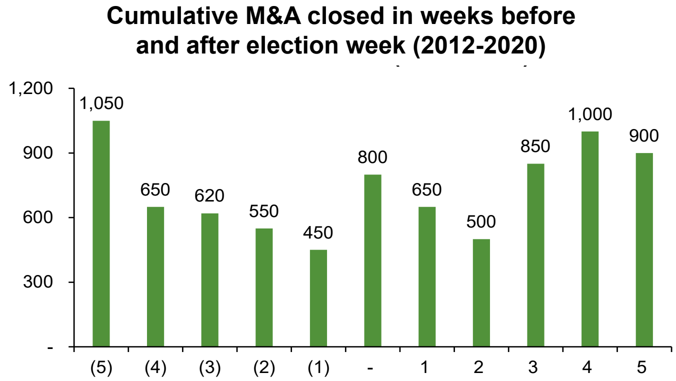


1. Source: CapIQ.

Further, in data sourced by PitchBook, we examined the 2020, 2016, and 2012 elections—excluding 2008 due to the global financial crisis—where it becomes clearer that M&A activity remains relatively stable around Election Day. Deal closings typically fluctuate between 400 and 1,000 per week, with no significant drop-off in the 11-week period leading up to or following the election. Historically, deal closings slowed in August and September, followed by a rebound in October and November, with a surge in deals closings in December. If 2024 were to follow this pattern, we can expect a similar increase in activity by year-end.

Average M&A closed in months before and after election month (2012-2020)



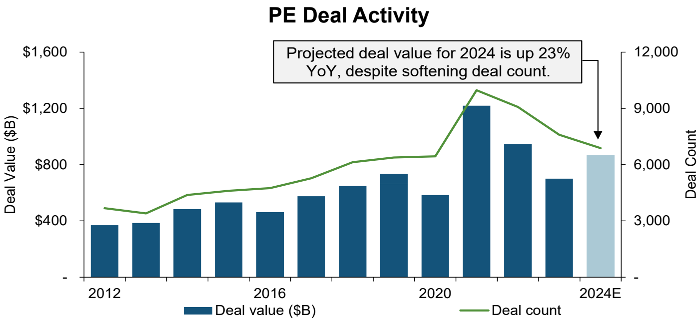


Given today's unique market landscape, it's important to recognize that the factors driving M&A activity now may differ from those of previous election cycles. Ultimately, this analysis indicates that M&A trends are more acutely influenced by macroeconomic conditions than by election cycles. When slowdowns occur, they tend to be short-lived, with M&A activity quickly regaining momentum.

Current Market Dynamics and the 2024 Election Cycle

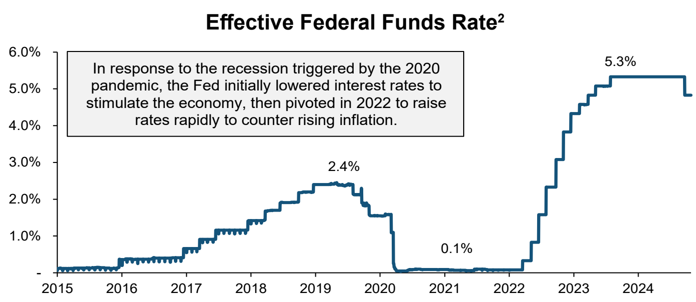
The environment we are navigating in 2024 is markedly different from the challenging conditions surrounding the 2020 election given the COVID-19 pandemic. Since 2022, increased interest rates, valuation gaps between sellers and buyers, geopolitical conflicts, and broader market uncertainties have created a more difficult landscape for M&A. If we take a closer look into 2024, the quarterly data suggests a potential shift. Overall, Q1 through Q3 of 2024 has shown improvement compared to the same periods in 2023 in the U.S., with a notable rise in add-on acquisitions through June. While these positive trends for the first half of 2024 are encouraging, they must be considered in the context of other factors impacting dealmaking. Several key indicators now point to a potential uptick in M&A activity moving forward, as detailed below.

1. **Increased Deal Value[1]:** In Q3 2024, U.S. private equity ("PE") dealmaking continued its robust recovery, despite heightened uncertainty surrounding the upcoming presidential election. Year-to-date, deal value has surged by 23.1% year-over-year and a 12.9% increase in deal volume. On its current trajectory, the industry is set to reach $864.3 billion in deal value for the year, which would mark the third-highest total on record. This recovery, following a two-year slump where deal value dropped 42.5% from peak to trough, reflects resilience in the face of political and economic volatility. The 2024 election could potentially introduce new headwinds, but recent PitchBook data for Q3 2024 underscores the sector's momentum going into the final months of the year.



1. Source: PitchBook. 2. Source: IMAA-Institute. Data includes U.S. M&A transactions. 2024E is annualized.

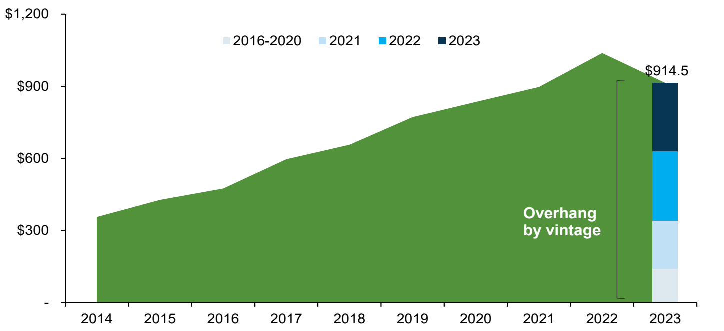
2. **Stabilized Interest Rates / Continued Cuts[1]:** After a period of aggressive interest rate hikes, the market has begun to stabilize, with the Federal Reserve implementing a 50-basis point reduction in September—its first monetary easing in four years. This marks a shift toward easier monetary policy and with continued conversations suggesting further reductions in 2025. Lower borrowing costs are expected to stimulate M&A activity by making financing more accessible for buyers. Regardless of the outcome of the upcoming election, this should restore confidence in more predictable monetary policy, encouraging dealmakers to take advantage of more favorable rates.



1. Source: JP Morgan Chase. 2. Source: FRED.

Election Cycles and the Impact on M&A Activity

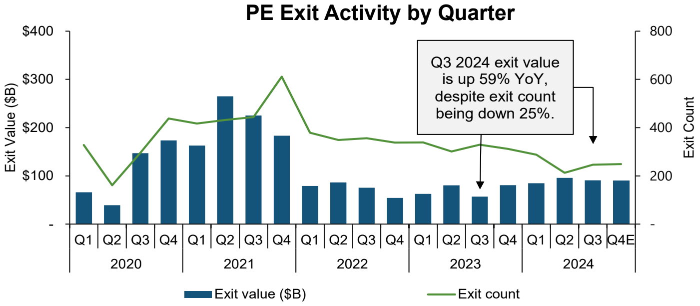
3. **Private Equity Dry Powder[1]:** The PE industry is sitting on a record $914 billion of dry powder—uninvested capital that has remained sidelined for an extended period. Investor pressure to deploy and return capital is mounting, driving a notable uptick in M&A activity, particularly in the realm of add-on acquisitions. As PE firms seek to scale their portfolio companies through strategic M&A, this accumulated capital is fueling more deals, even in today's cautious market.



1. Source: PitchBook.

4. **Private Equity Portfolio Exits:** Many PE firms are nearing or well past the end of their typical holding periods for portfolio companies acquired during the mid-to-late 2010s, with exits delayed due to macroeconomic constraints, particularly in larger middle-market deals ($1 billion+). This impending wave of exits will return capital to investors, effectively restarting the PE cycle of investing, harvesting, returning, and reinvesting.

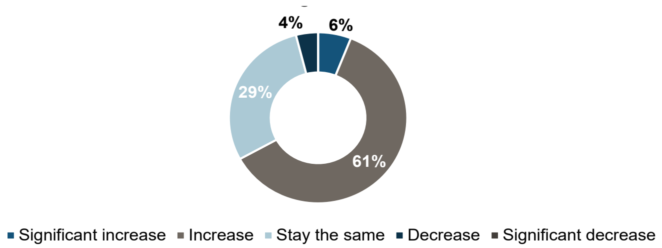
PE Exit Activity by Quarter



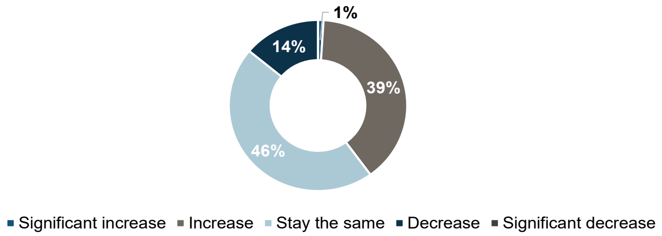
1. Source: BDO and Tax Foundation.

Despite the many positive leading indicators, the 2024 election adds another layer of uncertainty. Nonetheless, the recent uptick in M&A activity is reinforced by a Grant Thornton survey of M&A professionals, which predicts increased activity in the next six months compared to the previous six, as shown in the accompanying charts below. Additionally, when these professionals were asked about valuation expectations, 46% of respondents anticipated valuations would remain steady, with many expecting increases rather than decreases. However, valuation fundamentals are more complex than deal volume trends. Election-related uncertainty contributes to this complexity. On the supply side, private equity firms may accelerate portfolio company sales, and a potential glut of sellers could emerge post-election.

Q: Compared with the last six months, how do you expect deal volume to change in the next six months?



Q: How do you anticipate valuations changing in the next six months?



2024 Election Presidential Business Tax Plan Overview[1]

A central topic surrounding the election for business owners and prospective sellers is the potential impact of each candidate's tax proposals. This election highlights a clear contrast between the two major parties' approaches to taxation. The Tax Cuts and Jobs Act ("TCJA"), enacted in 2017, made corporate tax cuts permanent, while individual rate reductions are set to expire at the end of 2025. Current Republican proposals aim to make these individual cuts permanent, providing continuity for high-income earners and business owners. Democrats, by contrast, propose increasing taxes for individuals earning over $400,000 while keeping rates steady for those below this threshold, along with increased taxes on businesses. Here is Charter's comprehensive comparison of each party's business tax proposals, highlighting the possible implications for business owners and prospective sellers.

	Current Law	Harris's Proposal (Dem)	Trump's Proposal (GOP)
Business Taxes	Corporate rate is 21%.	Increase corporate rate to 28%.	Reduce corporate rate to 20%; to 15% for companies manufacturing in the U.S.
Capital Gains and Dividends	Top long-term capital gains rate is 20% for income over $518,901 ($583,751 for joint filers), plus a 3.8% net investment income tax ("NIIT") for income above $200,000.	Raise top long-term capital gains rate to 28% for income above $1M; NIIT rises to 5% for income over $400,000.	No new capital gains/dividend tax proposals.
Deductions	SALT deduction capped at $10,000 under the TCJA.	Increase small business startup deduction to $50,000; limit deductions on employee pay over $1M; limit deductions on rental investments.	Remove or increase SALT deduction cap.
Estate Taxes	Estate tax exemption for 2024 is $13.6M million. Step-up in basis allowed for transfers at death.	Tax unrealized capital gains at death for estates over $5M ($10M for joint filers).	Make TCJA estate tax reductions permanent.
Exemptions	Federal and state taxes apply to Social Security, tips, and overtime income.	Exempt tip income from taxation.	Exempt tip income, overtime pay, and Social Security benefits from taxation.
Payroll Taxes	12.4% payroll tax split evenly between employer and employee, applicable to income up to $168,600.	No direct payroll tax changes, but tip income would be exempt.	Exempt overtime, tip income, and Social Security benefits from payroll taxation.

While it's clear that two contrasting tax proposals could emerge from the 2024 election, business owners and prospective sellers should consider how each candidate's tax plan might affect their transactions. Regardless of the election outcome, both plans will face the complex federal legislative process, where negotiation and compromise may reshape each proposal. Given these uncertainties, business owners should remain adaptable, consult advisors, and strategically position themselves as tax regulations evolve with the political landscape.

1. Source: BDO and Tax Foundation.

Navigating M&A Strategies During Election Cycles

As a business owner considering an M&A transaction in today's environment, strategic preparation is key for positioning yourself for success. While political factors can influence market behavior, the broader economic climate—interest rates, inflation, and market stability—remains the primary driver of M&A decisions, as highlighted by the data.

Charter has observed a notable shift in transaction processes, particularly in the due diligence phase, where buyers are demanding more comprehensive insights into target companies' operations, market trends, and overall resilience. Sellers in turn are expected to provide enhanced transparency to build buyer confidence. In fact, a recent survey by Datasite reveals that the time required to prepare a deal rose by 27% in the first half of 2024 compared to 2023, highlighting this shift toward comprehensive scrutiny.

To help businesses manage these complexities, we've identified key characteristics that can strengthen M&A positioning during election cycles. With proactive measures and a focus on transparency, sellers can reduce transaction uncertainty and increase the likelihood of a successful transaction.

Develop a Strong Strategic Plan: Businesses pursuing M&A strategies should engage in strategic planning based on their specific transaction objectives. The first step is to form an internal task force, often including both internal and external advisors, who have a thorough understanding of shareholder goals. These objectives can range from maximizing enterprise value, tax optimization, and deal timing/certainty to close, to preserving the company's legacy and ensuring employee continuity. A dedicated team with clear communication channels enables more agile and informed decision-making, allowing the business to adapt quickly to changing economic and political conditions.

Engage with Advisors Early: Collaborating with investment bankers, legal, and accounting advisors is crucial when navigating the complexities of M&A during an election year. These advisors possess an understanding of the nuances involved in transactions and can provide invaluable insights into market dynamics and regulatory considerations. Given that most shareholders have only one opportunity in their careers to transact, it is essential to execute the deal effectively and strategically.

Consider Timing: Companies should carefully evaluate the timing of their deals in relation to the election timeline and anticipated policy changes. By understanding the regulatory environment and potential legislative shifts, businesses can make informed decisions about whether to accelerate or delay transactions. Strategic timing can optimize deal conditions, minimize risks, and enhance the likelihood of successful outcomes.

Proactively Prepare for Prolonged Due Diligence: With buyers conducting more in-depth due diligence in uncertain environments, it's important to prioritize financial and operational data. Clean, detailed records build confidence and expedite transaction timelines. Highlight recent performance metrics, stability measures, and growth initiatives to reinforce value and streamline the process.

By incorporating these strategies, businesses can effectively navigate the complexities of selling during an election year, positioning themselves for successful transactions even in challenging environments. While election cycles may introduce uncertainty, businesses that prepare thoughtfully can position themselves to leverage opportunities and achieve successful outcomes.

Conclusion

While election cycles introduce uncertainty into the M&A landscape, particularly regarding potential policy and tax changes, their overall impact on lower middle-market M&A activity tends to be more moderate than feared. Historical data from the last three election cycles suggests that M&A activity remains resilient, with only temporary slowdowns that recover by the end of the year. In 2024, we see a similar trajectory, with positive leading indicators—such as increased deal value, stabilizing interest rates, and high levels of private equity dry powder—pointing toward a strong finish for the year.

Although political uncertainty can add complexity to decision-making, macroeconomic factors play a far more influential role in shaping M&A activity. As we approach the 2024 election, businesses contemplating a transaction would benefit from proactive planning and expert advisory support. These elements will be essential for navigating the unique challenges of this election cycle and maximizing the potential for successful deals.

At Charter Capital Partners, we understand the nuances of election-year M&A and are committed to guiding you through these unpredictable periods with informed, strategic advice. With a clear understanding of the broader economic landscape, we help businesses capitalize on opportunities and mitigate risks, ensuring they are well-positioned for success regardless of the election outcome.

CHARTER Capital

About Charter Capital:

Founded in 1989, Charter Capital provides premier investment banking and private capital management services, focused on mergers, acquisitions, and growth financing. With independent-business agility and big-business reach, Charter Capital brings both the high-touch service and the deep industry expertise businesses need to succeed. The seasoned team tailors every engagement to meet the unique needs of its clients and investment partners, ensuring long-term success.

Learn more: chartercapitalpartners.com / chartergrowthcapital.com.

About the Author:

Justin Pinto, Vice President

Justin Pinto joined Charter Capital Partners in 2016 and currently serves as Vice President, previously holding roles as Senior Associate and Financial Analyst. Justin manages and executes M&A client engagements, with a focus on Charter's distribution and industrials practices.

His expertise spans merger and acquisition advisory, private capital raising, and strategic consulting, primarily for family-owned businesses in sectors like distribution, industrials, and healthcare. He has advised on transactions for companies ranging from $10 million to $100 million in enterprise value.

A Michigan native, Justin earned his BA in Business from Hope College in 2018. Actively engaged in his community, he is a member of ACG Western Michigan and the Van Andel Institute JBoard.

In his free time, Justin enjoys outdoor activities—boating on Lake Michigan in the summer and skiing out West in the winter. An avid Detroit sports fan, he cheers on the Red Wings, Lions, and Tigers. Always ready for a new adventure, Justin loves to travel and explore.

CHARTER CAPITAL PARTNERS
140 Monroe Center NW, Suite 300 • Grand Rapids, MI
chartercapitalpartners.com • 616.235.3555

M&A ADVISORY TEAM:

John Kerschen
President & Managing Director
jkerschen@chartercapitalpartners.com

Mike Brown
Partner & Managing Director
mbrown@chartercapitalpartners.com

Mike Palm
Partner & Managing Director
mpalm@chartercapitalpartners.com

Mark Streekstra
Partner & Managing Director
mstreekstra@chartercapitalpartners.com

Jenny Dakoske
Director
jdakoske@chartercapitalpartners.com

Zach Wiersma
Director
zwiersma@chartercapitalpartners.com

Elisa Berger
Vice President
eberger@chartercapitalpartners.com

AJ Ebels
Vice President
aebels@chartercapitalpartners.com

Justin Pinto
Vice President
jpinto@chartercapitalpartners.com

Michael Pohl
Associate
mpohl@chartercapitalpartners.com

Keegan Ensing
Senior Analyst
kensing@chartercapitalpartners.com

Travis Read
Analyst
tread@chartercapitalpartners.com

Dylan Stenzinger
Analyst
dstenzinger@chartercapitalpartners.com

Kevin Caballero
Analyst
kcaballero@chartercapitalpartners.com