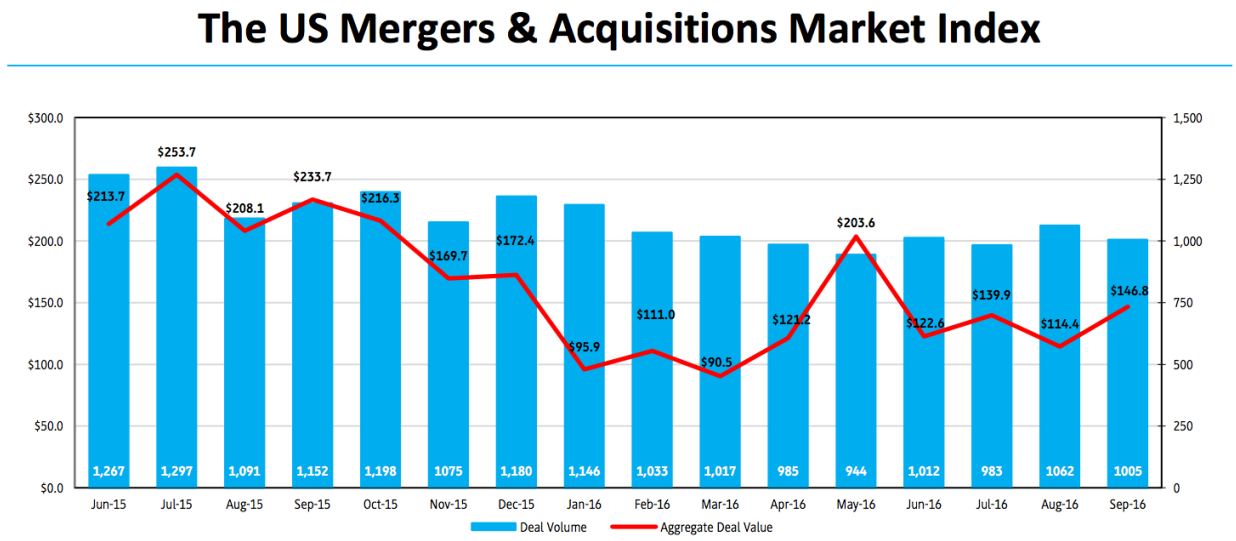
Deals, Deals & More Deals: A Red October for The Record Books

If you saw the cover of the Wall Street Journal this past Friday, there was a story about the potential partnership between two economic powerhouses. And no I am not referring to the heartwarming picture of Michelle Obama embracing Hilary Clinton. Instead, I am talking about the other partnership described just to the right of them, with the headline "GE Pursues Major Deal in Oil Patch."

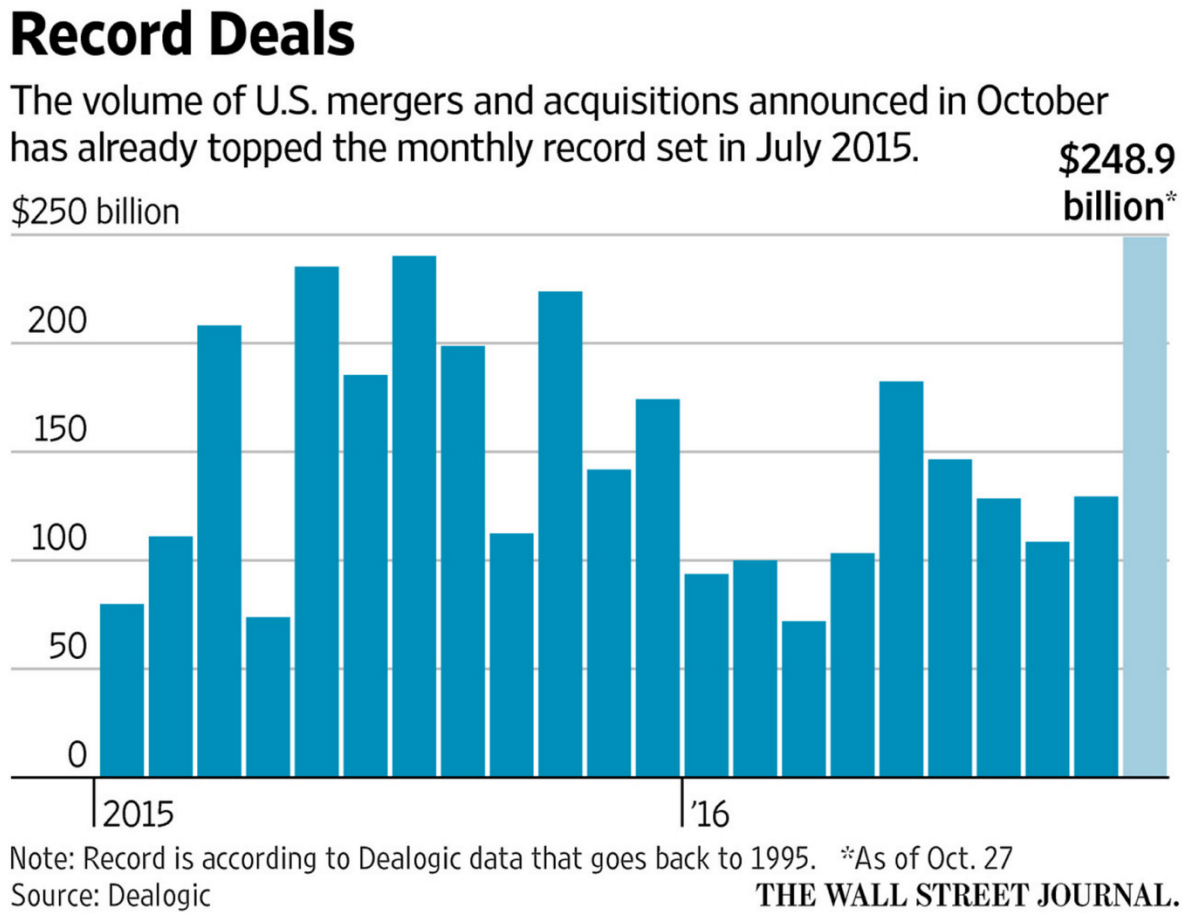
Last week it was reported that General Electric had approached Baker Hughes about a possible partnership that could be worth upwards of $20B. There is nothing really out of the ordinary here as public companies engage in a variety of mergers, acquisitions and joint-ventures all the time. What I do find particularly interesting is that despite today's unprecedented investment environment, mired by financial and geopolitical uncertainty, this October will mark the busiest month for M&A activity in the history of the United States. The figure below, from FactSet, illustrates the steady decline in monthly M&A activity since last summer.



Outside the $203B worth of deals made this May, monthly M&A transactions in 2016 have been sluggish at best. According to FactSet's most recent report M&A activity with exception to May, was less than $150B every month this year. This figure is down about 20% annually when compared with 2015 which averaged roughly $200B per month.

Only the truest of contrarians could have predicted that the month prior to the U.S. Presidential Election would garner such explosive M&A activity. Put all the arguments about lofty asset valuations, stagnant economic growth and peak earnings aside. Notwithstanding the impact of experimentally low interest rates, the eve of an election is typically not a popular time for decision-makers to go on shopping sprees. As they wait for the smoke to clear on the future of anti-trust policy it makes sense why businesses typically put deal-making to the side during the months preceding an election.

But as this year has been a first for many things, the M&A market has been no different. Market watchers can now add the week ended October 28th and its record $177B in M&A transactions just two weeks prior to the Presidential Election, to their growing list of 2016's market anomalies. See the figure below, provided by the Wall Street Journal. So far this October the aggregate deal value is almost $250B, breaking last July's record of $240B.



Long story short, the M&A space is absolutely flourishing lately. Does it make sense? No. Even at ultra-low interest rates last year's record-breaking annual M&A activity was suspect.

Could the forces driving this be two presidential candidates that are pro-business, thus companies are joining forces in anticipation of more favorable anti-trust policies? Actually, not at all. This year, even the right wing candidate, usually associated with free-market values, has been shooting out unfriendly tweets about the business practices of some of America's top companies, including Apple and Amazon. Despite being a self-proclaimed "deal-maker" himself, Donald Trump's campaign made the following statement last weekend in regards to the recently proposed takeover of Time Warner Cable, by Telecommunications giant AT&T for roughly $85B:

> *"Donald Trump will break up the new media conglomerate oligopolies that have gained enormous control over our information . . . Donald Trump would never approve such a deal."*

While Democratic candidate Hilary Clinton did not comment directly on the recent deal, she has made statements during her campaign hinting that she would be even tougher than the current administration regarding these massive deals. If elected, Hilary has vowed to "beef up the antitrust enforcement arms of the Department of Justice and the Federal Trade Commission."

According to a Financial Times article written earlier this year, as of April of 2016 the Obama Administration had blocked $370B worth in deals since 2009. Most infamous of course, was the proposed tax-inversion deal between Pfizer and Allergan for about $160B, that was eventually abandoned by the two companies due to political pressures.

The administration has already blocked proposed take-overs of both Time Warner Cable and Baker Hughes over the last year due to anti-trust concerns. Interestingly enough, both companies have recently re-emerged in M&A talks with brand new partners this past week. I guess the lesson here is that as long as it makes enough economic sense for a company to be taken-over within all practical anti-trust concerns, there is only so much the government can do to stop it.

With corporate earnings growth basically flat for years now, many companies have been forced to look externally for new opportunities. While this boom in M&A activity is coming at a very unique time by any historic measure, regardless of how you wish to make sense of it this type of deal-making activity is a positive sign for markets. During Q1 of 2016 the S&P 500 broke its annual record for share buybacks and along with it drew much criticism about the lack of alternative investment opportunities. Fast forward just a few months later and the market seems to have got exactly what they asked for.

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