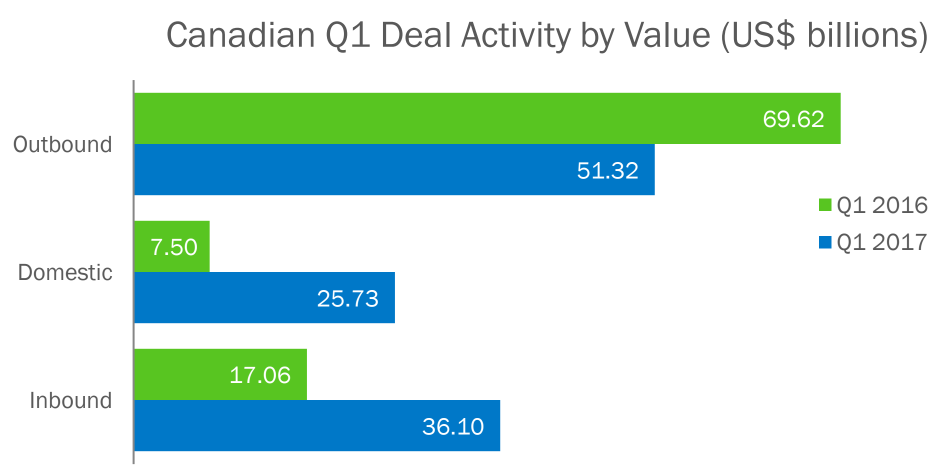
The Uncertainty of the Deal: US Trade Policy and Canadian M&A

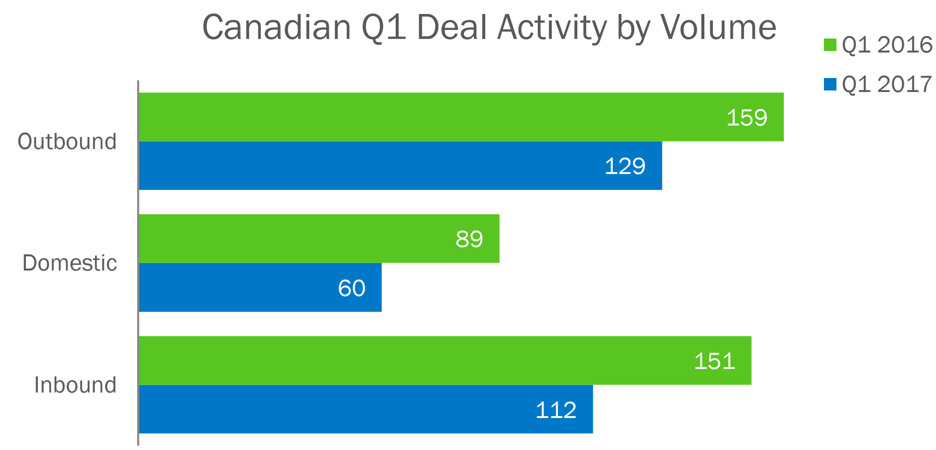
In the opening pages of *Trump: The Art of the Deal*, Donald Trump describes his work style:

"I play it very loose…I prefer to come to work each day and just see what develops."

This approach was recently highlighted in President Donald Trump's rumblings about trade policy with Canada. Last week, after a visit to Wisconsin, he remarked that "[i]n Canada, some very unfair things have happened to our dairy farmers, and others, and we're going to start working on that." This was followed by an announcement that a tariff of approximately 20% would be imposed on Canadian softwood lumber imported to the U.S.. And then came media reports that Trump was going to sign an executive order withdrawing the U.S. from NAFTA, a plan that was reversed after emergency calls with Mexican President Peña Nieto and our own Prime Minister Trudeau. Thursday morning, President Trump tweeted: "Relationships are good – deal very possible!". It's been quite a couple of weeks.

Where does this trade policy uncertainty leave us in Canada? What are the implications for our own economy, and more specifically, for Canadian M&A deal activity? Looking back at Q1, 2017, announced deal activity followed the broader North American trend of higher deal value and lower volume. Inbound deal value was notably higher in 2017, but inbound deal volume declined, and if we remove mega-deals (US$1B+) from the equation, inbound deal value and volume declined by, respectively, 23.6% and 26.7%.





In addition to broader market factors (an abundance of dry powder competing for a shrinking pool of quality targets), the uncertainty of U.S. trade policy is a factor for Canadian investment activity[1]. The softwood lumber tariff announcement aptly illustrates this point. Following the announcement of the tariff, Canadian lumber stocks West Fraser Timber Co. Ltd. And Canfor Corp climbed, respectively, 8.8% and 7.9%, making these stocks the "biggest movers on the S&P/TSX composite index" this past Tuesday[2]. Investors were apparently expecting worse, and providing some clarity shifted expectations.

During a recent webinar on "How Protectionist Attitudes impact the M&A Market", the consensus view was that potential costs on exporting to the U.S. represent the biggest concern for Canadian M&A activity. At this point, however, it is not clear what, if any, form these will take. In an effort to shed some light on this uncertainty, I asked the opinion of a respected Boston attorney who specializes in cross border trade. His answer…"it is too early to tell".

I wish I could end this article with a clearly defined message about U.S. trade policy and how it will impact Canadian M&A. Where a Canadian target exports to the U.S., potential acquirers should certainly consider the cost of U.S. assembly, in the event that onerous taxes or tariffs are imposed. But for now, when it comes to the direction of U.S. trade policy, to quote President Trump, we will "just [have to] see what develops."

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[1] The Bank of Canada continues to highlight this point. For example, see http://www.bankofcanada.ca/2017/03/getting-down-business-investment-economic-outlook/

[2] The Globe & Mail, April 25, 2017