CORPORATE VALUE PARTNERS
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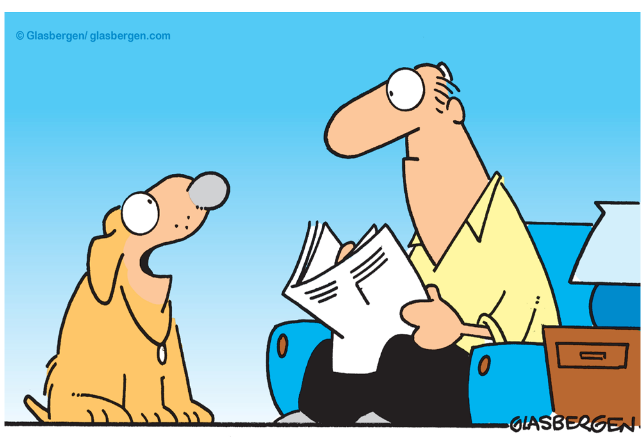
Politics and Valuation

Summer and Fall are my two favorite seasons, except every fourth year for the presidential election. Then I count the days until it is over, and everything can get back to normal. Too much of the communications during the election cycle are far too combative and completely lacking in useful information. It's all just too much.

But I always find myself trying to dig through the noise to understand the general trend of the campaigns. That can take some work, but from a business and valuation perspective it can be useful. That's because the campaigns can give insights into how their policies may affect the economy and the business environment in the future. As I've written in prior newsletters, valuation is a prophecy of the future, so it helps my work if I understand where things may be headed during the next four years.

Be Like Yoda

The most important thing I try to do is to separate emotionally from the messages the campaigns send. That is difficult to do, because both campaigns have people that are very talented at crafting messages meant to generate an emotional response (such as vote for me, give me money, or more common lately - despise my opponent). It is hard to stay cool and calm, but if I can there are often useful bits of information that I can work with.



"Everywhere I go, people are eager to shake my hand and shower me with compliments. With that kind of charisma, I'd be crazy not to run for office!"

Even more generally, though, a detached mindset is helpful to a valuation analyst's work. Regardless of what an analyst might prefer, they have to remove their personal biases and see things just as they are, not as they want them to be. That goes for all aspects of the valuation assignment, not just those that touch on politics. An unbiased understanding helps an analyst develop assumptions that better reflect economic reality. Ultimately, that is what we try to do as valuation analysts – capture economic reality.

Indirect vs. Direct Impacts

As an example, a common point of disagreement in presidential campaigns is tax policy. At the highest level, tax policy will have an impact on government tax receipts, debt levels and economic growth. Government tax receipts and debt levels will affect capital markets, which could put upward or downward pressure on interest rates and economic growth, depending on the policy. While these matters affect a company indirectly, they will affect its value.

But tax policy can also have a more direct impact on the company that is being valued. As I have mentioned in prior newsletters, we focus on after-tax cash flows when valuing a company. Changes in future tax rates, up or down, will affect after-tax cash flows, which has a direct impact on a company's value.

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Another common point of disagreement is trade policy. At the highest level, trade policy can have an impact on overall economic activity, which affects GDP growth, government tax receipts, debt levels, employment levels and consumer confidence, among others. Again, these matters have an indirect impact on the company being valued.

However, trade policy can have a direct impact on a company that is being valued, particularly in certain industries. If a company is in an industry that is subject to tariffs, or some sort of trade dispute, their sales and cash flow could be dramatically affected either positively or negatively, depending on the candidate and their proposed trade policy.

There are many other examples. Whenever one political party or another wants to make a big change in some way, it is up to us to sift through the messages to see what is likely to happen, and how that will affect the value of a company. The important thing is to cut through the noise and look for the underlying economic reality. If we can capture economic reality, we get closer to developing a more reliable estimate of value.

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