Shareholder Activism in a COVID-19 World: Past, Present and Future

"All it takes is a single activist to have a more optimistic view than the market and a belief that their ideas will help to close a perceived gap between price and value," write Sidley Austin's Derek Zaba and Kai Liekefett. "With this backdrop, general counsel and their legal teams would be wise to consider how prepared they are for activism in a COVID-19 world."

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As the COVID-19 pandemic began to unfold in early March, it quickly became clear that the crisis would act as a “poison pill” that would sharply reduce shareholder activism in the spring. Initially, many activists were preoccupied with their own survival and/or attracting new capital rather than launching new campaigns. Additionally, it became difficult to obtain shareholder support for public activist campaigns at a time when boards and management teams were focused on managing through the immediate crisis.

In addition, conditions were ripe for a surge in adoptions of poison pills, formally known as shareholder rights plans. For many companies, responding to stock prices that had collapsed 50% or more in a matter of days was a component of managing through the crisis. At the same time, equity trading volumes had increased and thus an activist or potential hostile acquirer was able to accumulate a large stock position quickly. Additionally, the increased volatility and general upheaval in the equity markets resulted in atypical trading patterns (and other behaviors), diminishing the effectiveness of traditional stock watch methods to identify activist accumulations that rely on pattern recognition.

In the first few weeks of the crisis, more than a dozen pills were adopted. Shortly thereafter, proxy adviser firms Institutional Shareholder Services (ISS) and Glass Lewis both published guidance indicating greater acceptance of short-duration poison pills in the current circumstances. For example, ISS’s April 8 guidance specifically noted that “[a] severe stock price decline as a result of the COVID-19 pandemic is likely to be considered valid justification in most cases for adopting a [one-year] pill.” As a result, approximately 50 companies adopted “poison pills” by mid-May. To further put this number in perspective, only 25 S&P 1500 companies had a poison pill in place at the end of 2019, according to FactSet.

However, as the equity markets have bounced back and volatility has subsided, both issuers and shareholder activists are transitioning to the next phase in the rapidly evolving shareholder activism landscape. Management teams have removed their firefighter gear and begun to consider the longer-term implications of the COVID-19 crisis. This is evident in the trends of poison pill adoptions: in June and July, fewer than 10 poison pills in total have been adopted, which is a far cry from the pace of adoptions in prior months.

Likewise, activists have begun to look past the summer and are preparing for the fall and winter. Many have or are building positions and are reaching out to the companies that are next on their current hit list. After being forced to the sidelines during proxy season, many activists are anxious to prosecute campaigns. Companies with director nomination deadlines in the early fall or whose governing documents permit shareholders to call a special meeting or act by written consent are particularly vulnerable in the current environment. It is also not necessarily the case that strong stock price performance protects you. Certain industries, such as many in the technology sector whose businesses are largely insulated from the most deleterious effects of a continued COVID-19 crisis, offer safe(r) haven to investors, including activists. Many of these industries also happen to be those where customer behavior and industry dynamics have been most disrupted by the COVID-19 crisis, resulting in an increased possibility of a divergence between the current stock price and an individual investor's assessment of intrinsic value. All it takes is a single activist to have a more optimistic view than the market and a belief that their ideas will help to close a perceived gap between price and value.

With this backdrop, general counsel and their legal teams would be wise to consider how prepared they are for activism in a COVID-19 world. In doing so, they should ask themselves the following questions:

- **Understand the attractiveness to an activist of your business in the current environment.** Has your stock price been disproportionately impacted versus your business? Has your stock performed reasonably well but the crisis changed the strategic appeal of the company to a potential suitor?
- **Understand your governance vulnerabilities.** Beyond understanding your business, strategic and financial vulnerabilities, what are possible attacks on your board, compensation, ESG and other governance issues? Has an activist law firm reviewed these issues from a proxy fight perspective?
- **Develop an activism response plan and assemble a team.** If an activist publishes a 100-page white paper or calls your CEO's private phone number to announce their presence, what are your initial steps? How quickly can you assemble your key internal constituents and external advisors to respond appropriately?
- **Have an up-to-date shareholder rights plan "on the shelf."** This entails conducting the proper diligence and drafting the necessary documentation to ensure that a poison pill could be adopted immediately upon the identification of a threat. If there is another swoon in the equity markets, are you prepared to implement a rights plan overnight if warranted?
- **Review your bylaws and other governing documents.** Are your bylaws and other governing documents up to date with constantly evolving activist tactics?

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