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Hostile Takeover Bids on the Rise in 2021 — Will You Be Ready?

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The market looks ripe for an increase in hostile takeover bids. Knowing the warning signs that your company may be vulnerable is the first line of defense.

Most everyone in business knows the famous quote from the ancient Chinese general Sun Tzu: “If you know the enemy and yourself, you need not fear the result of a hundred battles.” As familiar as that may be, when it comes to defending your company from an unsolicited takeover bid, it packs an eternal punch.

Heading into Q2, signs in the market point to disruptive forces hungry to acquire coveted assets. The availability of capital and number of prospective purchasers seeking deals makes hostile bids more likely by aggressors. In some cases, activist investors are teaming up with aggressors in lieu of taking their issues directly to the shareholders of the target, where proxy fights seek to install dissident directors who are more friendly to a deal than incumbents.

What’s behind this trend? Simply put, many public companies are ripe for picking. Record highs in the major market indices have masked the fact that companies have not participated in recent expansion in private equity multiples. These stragglers are unloved — and often undervalued, particularly when measured from the highs prior to the onset of the pandemic in March 2020.

When coupled with an overabundance of dry powder in the form of available capital plus challenges in some industries to find meaningful levels of organic growth (at least during COVID-19), conditions are optimal for hostile takeover activity.

Of course, there can be other motives for an unsolicited hostile bid. Failure to generate organic growth is always a significant factor, no matter the market conditions. Ego can also play a big role.

Whatever the reason, the current climate means that boards and management teams need to watch their backs and be ready for the possibility of an unsolicited takeover bid or other, seemingly milder tactics, such as proxy contests.

Keep an Eye on Your Stock

Like the Sun Tzu quote suggests, knowing as much as possible about your company can help you defend against a hostile campaign — both before one occurs and during.

One starting place is to monitor your shareholder base to avoid surprises, such as the unexpected filing of a Schedule 13D with the SEC once a shareholder beneficially owns 5% of your stock. One valuable tool is to utilize a stock surveillance service that closely tracks both the company's stock and its shareholders. It can help you keep an eye on the inside game to monitor activity that could eventually result in a 13D filing. Stock surveillance can serve as an early warning system of sorts.

A stock surveillance service provides real-time knowledge of the shareholder base and is especially valuable when facing a contested M&A situation. In these instances, aggressors often will acquire a "toe hold" in the target company as a first step in the takeover process. Informed and updated equity-flows data within the shareholder base is critical to identifying early action and estimating how many votable shares an investor holds within their portfolio.

In contested instances, groups of investors, often with a common bond or link, join together in "wolf packs" to coordinate efforts in favor of the aggressor. They usually have a history of building positions in similar equities that have experienced an unsolicited bid or have faced demands from a shareholder activist.

Tracking positional moves of these investors and getting real-time updates on shareholder activity gives you "first mover" advantage. Knowledge of derivatives strategies and hedge fund accumulations in the early, non-public stages of a hostile campaign can be valuable in developing an effective game plan.

Your Secret Weapons

If a takeover bid is pending, there are points to consider for the battle ahead. Shareholders will need to determine whether the bid is in the best interests of the growth prospects of a potentially newly formed company. Alternatively, holders may want to consider whether to accept cash for their shares in favor of the long-term prospects offered by the current management and board.

Ultimately, the board and management team of a target need to smoke out the true intentions of the aggressor while also learning the risks and vulnerabilities of the bidder. In many hostiles, for instance, the aggressor may recognize its own inability to generate meaningful organic growth and be on the hunt for inorganic options to mask this issue.

In some cases, the takeover bid is done in the name of synergy, suggesting that the combination of the two companies creates value. In others, banding together complimentary products, services or technologies that result in improved operating performance and multiple expansion is the goal.

This is where business intelligence and forensic accounting can be valuable. The information that turns up can illuminate the leadership history of the nominated board members and help shareholders understand the successes, or failures, of these individuals in prior roles with other companies.

Are there claims of organic growth and successful integration of a previous merger? The collected information can shine a bright light here — empirical evidence and data go a long way in debunking myths. In turn, the information provides shareholders with a historical manifest of what to expect should the present bid succeed. To quote another legendary military leader who knew a thing or two about strategic hindsight, U.S. General George S. Patton, "Prepare for the unknown by studying how others in the past have coped with the unforeseeable and the unpredictable."

The favorable conditions for hostile bids make it incumbent on management to be prepared and to avoid surprises. It's important to know where your company stands and who is accumulating shares. Early identification of activity and monitoring recent investors in the stock are both valuable warning signs. When management is forewarned and forearmed, employing your best defense at the right time can impact the outcome.

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