

## MARKET REACTION TO POISON PILL ADOPTION

For 30 years, companies have adopted poison pills as antitakeover defenses, with research suggesting poison pills can be viewed as negative (entrenchment of poor management) or positive (receipt of greater takeover premiums). To respond to poison pill concerns, companies began adopting poison pills for specific purposes – either to protect net operating losses (NOLs) for tax purposes, or to extract greater takeover premiums when a takeover bid has been made. Recent research in the *Journal of Management* explores whether the stock market reacts to the adoption of specific-purpose poison pills differently than routine poison pills.

### Key Takeaways:

- Market capitalization is reduced by \$22.03 million upon poison pill adoptions to protect NOLs and increases by \$13.43 million when pills are adopted after a takeover offer.
- The company's strategy and corporate governance influence investor response by shaping interpretations of how poison pills will serve investor interests.

The authors examined investor reactions to 578 poison pills adopted between 2002 and 2011 and report that poison pills adopted to protect NOLs resulted in a 2.1% decrease in their share price compared to routine poison pill adoptions, but pills adopted after a takeover offer saw an increase of 1.28%. In the data, such differences amounted to a loss of \$22 million or gain of \$13

million. Further, governance and strategic characteristics influenced the market's response. For NOL poison pills, the market responded more negatively when the company had higher prior investments in R&D (\$558 million loss for one standard deviation above average). For poison pills adopted after tender offers were received, investors responded more positively when the company had: 1) a separate chairman and CEO (\$33 million), 2) more inside executives on the board (\$32 million), 3) greater investment in R&D (\$18 million), and 4) a more concentrated industry environment (\$43 million).

In summary, specific purpose poison pills serve as a means of signaling positive intent to investors, but they are not always received positively. Investors consider additional factors in interpreting why management chooses to adopt such provisions. Managers should be aware of how decisions are framed and how prior actions may influence stakeholder interpretation.

Source: Schepker, D.J., Oh, W-Y., & Patel, P.C. (Forthcoming). Interpreting equivocal signals: Market reaction to specific-purpose poison pill adoption. *Journal of Management*, DOI: 10.1177/0149206316635250.

