



■ **ROUNDTABLE** February 2019

SHAREHOLDER ACTIVISM AND ENGAGEMENT

Shareholder activism continues to thrive and expand in scope and type of activist. Across the globe, activists are busy choosing their targets, preparing their campaigns and honing their attack strategies. And with shareholder activists increasingly able to have multiple company directors replaced, boards are becoming more cognisant of this eventuality and, as a result, are proactively communicating with shareholders, studying their vulnerabilities and engaging with activist agendas. ■



THE PANELLISTS



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Charles A. Koons is managing director of the activism and contested situations advisory group at Morrow Sodali. He has over 23 years of experience as a trusted adviser in proxy contests and M&A to both corporate issuers as well as shareholders, previously as managing director of MacKenzie Partners. He provides year-round as well as special situation counsel to companies on how to best position themselves within the investor community.

FW: What do you consider to be the most significant developments in the shareholder activism space over the past 12 months or so?

Koons: While 2018 did not see the prevalence of mega-cap fights of 2017 like Proctor & Gamble, ADP, Arconic and General Motors, it was still a very busy year for activists with high-profile engagements at targets such as Newell Brands and Campbell Soup. 2017 was the first time that more than 50 percent of activist engagements occurred outside of the US. Elliott is a prime example of an activist who is comfortable working in an extremely wide range of geographies. While some countries will continue to be less hospitable to activism than others, the globalisation of the ownership base of larger companies creates an inexorable movement toward greater transparency between shareholders and the companies in which they invest. In the US specifically, it remains to be seen what changes will come out of the US Securities and Exchange Commission (SEC) Roundtable that took place in November 2018. This very important discussion focused on key aspects of the US proxy system, including proxy voting mechanics and technology, the shareholder proposal

process, and the role and regulation of proxy advisory firms.

FW: What are some of the common issues being raised by activists? What factors are driving campaigns?

Koons: Common themes are the need for improved performance through better management and board oversight, return of capital to shareholders, opposition to previously announced M&A deals, support for the sale of the company to a strategic or financial buyer, and support for divestitures or spin-offs of one or more corporate divisions. In addition to these strategy and governance related themes, many activists such as ValueAct and Jana are bolstering their case for change at the companies they target with issues surrounding long-term sustainability. The most experienced activists do a great deal of research on the target company as well as its shareholder base prior to engagement.

FW: Are any sectors or industries particularly vulnerable to being targeted by shareholder activists? If so, why?

Koons: Combined, the technology, industrials and consumer sectors accounted

for almost 60 percent of the capital deployed in new activist positions through the third quarter of 2018, a significant jump from the average of 2015-17. We expect that market volatility, especially around the technology sector and its capital allocation, to contribute to more instances of activism. Many long-established industrial companies that are still grappling with their transition to the 21st century global economy have seen challenges to their board composition, as well as demands for greater clarity around the business structure.

FW: Looking around the globe, which countries and regions appear to be hotbeds for activism? Are there parts of the world where interest in activist strategies is clearly rising?

Koons: While activism in the US will not recede in the foreseeable future, recent market volatility globally will only present more opportunities for activists. Activists have not been deterred from expanding into geographies that previously have seen little or no shareholder activism. The UK continues to be the dominant target for activists in Europe, accounting for just over half of all engagements. We may well see a number of mega-cap European

companies targeted in 2019. In Asia, there is continued evidence of the movement away from the traditional passive approach to investing. The growing ownership share of Asian equities by foreign investors, as well as a more open approach to activism by local investors, has made the overall climate in Asia, and Japan in particular, more hospitable to activism and overall governance reforms.

FW: Have any recent shareholder activist campaigns caught your eye? What lessons can we draw from the way they were conducted, as well as their outcome, such as board-level resignations or strategy changes?

Koons: Recently, Newell Brands faced a proxy fight by Starboard Value Fund to replace the entire board of directors at the 2018 annual meeting. Newell was faced with the challenging circumstance of the departure of a substantial minority of its board and a stock price that was off significantly year over year. Through vigorous engagement with the shareholder base, the company ultimately was able to reach a settlement whereby representatives of both Starboard, as well as Icahn Enterprises, were added to the board, bringing in a strong shareholder perspective. Management and the board demonstrated a willingness to adapt and make necessary changes to be responsive to their shareholders in order to best position the company for long-term success.

FW: What insights can you provide into the various approaches activists are taking to exert their influence and effect change? To what extent have tactics evolved in recent years?

Koons: More sophisticated activists are spending time in and around the wider investment and governance community to understand the focus and priorities of funds such as BlackRock, Vanguard and State Street. The increasingly large ownership that these index funds have in most mid-cap and larger companies makes their votes pivotal to the outcome of a contested election. Understanding how these funds

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think about governance and long-term sustainability is key to winning their vote. Larry Fink's letter of January 2018 to CEOs of major corporations stated that boards of directors must articulate clear goals to achieve long-term growth.

FW: How are legal and regulatory developments affecting this space? To what extent do shareholder-friendly laws, for example, facilitate activism and make campaigns more likely to succeed?

Koons: An activist's ability to succeed in a campaign is directly tied to their ability to identify and connect with their fellow shareholders, as in any campaign. Access to the shareholder data varies greatly from region to region. In Australia, an activist will be able to see the entire shareholder registry, while in other parts of the world the shareholder base is much more opaque. The US system has traditionally been a complicated mix of institutions, custodian banks, beneficial owners and registered shareholders that an activist must navigate to be successful in a proxy contest. One area of potential change that the SEC panel discussed at the November roundtable was around the 'NOBO-OBO' framework, whereby the identities of a significant portion of the beneficial shareholders are currently not directly visible to the company or an activist. A change to this framework

that would allow complete transparency would significantly alter the playing field.

FW: What can companies do to proactively monitor the market, identify red flags and anticipate the onset of an activist campaign?

Koons: All companies should have an experienced outside team to monitor the trading and the shifting landscape of their shareholder base. An experienced team will be able to spot unusual trading activity and, in many cases, identify its origin. Stockwatch has many similarities to submarine warfare. Since trading in public shares is done in a less than transparent manner 'under the surface', it takes a skilled and experienced analyst or 'sonar man' to understand if the big block trade that just settled was an activist accumulating shares or simply a mutual fund doing some portfolio rebalancing. Investor relations needs to be more than a once a quarter function of an earnings call followed by questions and answers from investors.

FW: What strategies should companies consider to reduce the likelihood of becoming embroiled in an activist campaign? What shareholder engagement methods might be deployed, for example?

Koons: Preparedness for shareholder activism can be compared to foreign policy. The greater your level of engagement and diplomacy in times of peace, the greater likelihood that you will be able to avoid times of conflict. The three things a company should focus on are, first, know your owners. It is important to closely monitor your stock ownership and stay informed on the differing perspectives and priorities of your various shareholders. This will inform your shareholder engagement strategy to both investment and governance personnel, which should cover long-term strategic issues that are likely to be areas of focus for an activist. Second, know your company. You must have an honest and objective sense of how your company is performing in relation to its stated objectives and peers, as well as how your board and management are contributing to that performance. Third, know your team. Having a collaborative team of outside advisers that knows your company intimately will help you in your year-round engagement and evaluation process, thus positioning you to minimise the threat of

activism and to maximise your chances of being successful should such a threat become unavoidable.

FW: With social media now a powerful tool used by activists, how can companies derive benefits from these platforms to achieve their own objectives?

Koons: The tactics employed to reach retail shareholders are quickly evolving. We have seen activists mail individual video players to garner votes in a proxy contest as well as companies send instant messages with voting instructions via Facebook. The ability to produce video content geared toward retail shareholders quickly and inexpensively has given activists, as well as companies, new means by which to articulate and amplify their messages. The irony of our interconnected world is that it is more challenging than ever to get people's attention. Companies, as well as activists, need to be creative in order to make their messages stand out from the daily noise of our lives.

FW: Looking ahead, how do you expect shareholder activism to evolve? Are campaigns set to ramp up the pressure on boards, challenge corporate strategy and transform company culture?

Koons: Shareholder activism will continue to expand to new geographic regions as the trend toward the globalisation of the shareholder base accelerates. Shareholders of all types will demand greater insight into a company's long-term strategic vision. Market volatility will only present more opportunities for activists to accumulate substantial ownership positions in target companies and be in position to make the case for change to their fellow shareholders. Corporate boards must demonstrate to their investors that while they are comprised of a diverse mix of skills, experience and points of view, they agree upon a long-term strategic vision for the future of the company they oversee. Failure to articulate this vision will invite the engagement by a shareholder activist. ■