

# THE ACTIVIST INVESTING ANNUAL REVIEW 2019

THE SIXTH ANNUAL REVIEW OF TRENDS  
IN SHAREHOLDER ACTIVISM



Schulte Roth & Zabel

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Visit our Shareholder Activism Resource Center:  
[www.srz.com/Shareholder\\_Activism\\_Resource\\_Center](http://www.srz.com/Shareholder_Activism_Resource_Center)

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# SCHULTE ROTH & ZABEL FOREWORD

MARC WEINGARTEN, ELE KLEIN, ANELIYA CRAWFORD, AND BRANDON GOLD.

## INCREASING TRACTION

In the case of activist investors, success breeds success. As activists continue to secure board seats and strategic and operational improvements in the United States, developments in European activism have accelerated. Companies targeted by activists have become more likely to settle rather than risk losing a costly proxy fight. And activists have embraced M&A-related strategies to increase share prices.

## INCREASE IN EUROPEAN ACTIVISM

Though boardroom battles and proxy contests are often associated with American companies, activists ran campaigns against 148 European issuers in 2018. In part, this may be due to the European Union's recent directives encouraging shareholder participation.

Elliott Management led all activists with a record nine public campaigns launched at European companies throughout 2018. These efforts resulted in a number of favorable outcomes for Elliott, including gaining control of two-thirds of the board seats at Telecom Italia and a campaign alongside Sachem Head Capital Management resulting in Whitbread selling its popular Costa Coffee chain. European-based activists have grown alongside the increasing number of European targets and our London-based activist practice has been busier than ever. Notably, we helped our client Cevian successfully urge Autoliv, a company founded and headquartered in Sweden, but incorporated in the United States, to spin off its electronics segment, Veoneer, and gain a seat on the new company's board.

## ACTIVIST SETTLEMENTS

In 2017, companies seemed more reluctant to settle with activists, leading to a number of high-profile proxy fights that culminated in the largest contest in history at Proctor & Gamble, where we advised Trian Partners in securing a board seat. However, companies took a different approach in 2018, often choosing to settle with their activist shareholders rather than engaging in drawn-out campaigns. Third Point's

headline-grabbing campaign at Campbell Soup ended with Dan Loeb's fund obtaining two board seats and a mutually chosen third director. Our client JANA Partners' settlements resulted in two directors at each of Bloomin' Brands and Jack in the Box. Even first-time activist and client SRS Investment Management added two new directors to Avis Budget Group's board of directors, in addition to the two directors it already had on the board.

Whether the trend of activist settlements continues remains to be seen. But one certainty is that public companies have accepted activist investors as important shareholders, and have taken increasing efforts to seriously consider, and often accommodate, their suggestions. This likely will result in a large number of activist settlements in the years to come.

## THE YEAR OF M&A ACTIVISM

2018 showed an uptick in M&A-related activism. Activists frequently spoke publicly against acquisition offers that they felt undervalued targets, with the goal of getting a fair price for shareholders. For example, Carl Icahn and our client P. Schoenfeld Asset Management opposed an offer from Dell to buy its VMware tracking shares, citing an insufficient price. Icahn later agreed to a deal when Dell increased its offer and had the support of Elliott and Canyon Capital. Similarly, Icahn opposed an initial take-private offer for AmTrust Financial—the deal was later approved by shareholders at a sweetened price.

In a related strategy, some activists encouraged public companies to put themselves up for sale. Elliott, one of our busiest activist clients, offered to purchase athenahealth and urged the company to explore a sale. Later this year athenahealth entered into an agreement to be acquired by Elliott and Veritas. M&A-related activist strategies were particularly effective in 2018 and we expect these investments to continue in 2019.

Spurred on by a successful year of shareholder activism, it appears that activists will continue to encounter favorable results in 2019. 📌



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#### DEFINITIONS:

##### Primary focus:

A fund or individual which dedicates most, if not all of its assets to activist positions.

##### Partial focus:

A fund or individual which often employs activist tactics yet also uses other investment strategies.

##### Occasional focus:

A fund or individual that adopts an activist stance on an infrequent basis.

##### Engagement focus:

Typically large institutions and individuals that rally for change to promote good corporate governance.

##### Concerned shareholders:

An individual or group of individuals who collectively form a group of shareholders to enforce change, typically as a 'one-off' situation.

**M&A demands** include push for merger/ sale to third party, push for acquisition of third party, oppose merger/ sale to third party and oppose acquisition of third party.





# 2018: AN OVERVIEW

AFTER LAST YEAR'S FIFTH ANNIVERSARY CELEBRATION, THE ACTIVIST INVESTING ANNUAL REVIEW MUST WORK EXTRA HARD TO FIND NEW THINGS TO SAY ABOUT ACTIVISM. FORTUNATELY, ACTIVIST INSIGHT'S GROWING PRODUCT SUITE DOES THE HEAVY LIFTING, WRITES EDITOR-IN-CHIEF JOSH BLACK.

With the launch in 2018 of *Activist Insight Governance*, a new database of bylaws and directors; a major update to *Activist Insight Vulnerability* that allows for company-to-company comparisons; global stock price tracking; and a major retagging of board representation and M&A demands on *Activist Insight Online*, 2019 promises to be an exciting one for subscribers to Activist Insight.

The pages of this review highlight the depth of information on offer: from the more than 800 activist directors currently serving on U.S. boards to the number of bylaw amendments each year at Russell 3000 companies; the 922 companies targeted worldwide in 2018 to the 207 settlements involving board seat changes; the “bump” obtained by activists opposing deals; and the many successful predictions of *Activist Insight Vulnerability*. While we expect to share some of these insights across our platforms, including more in-depth articles in *Activist Insight Monthly* and *Activist Insight Online*, only by taking all five can users fully benefit from everything on offer.

## THE BIG PICTURE

A brief glance at activism in 2018 shows that, after a brief dip in 2017, things are back on track. The number of companies publicly targeted hit record highs in the U.S., Canada, Japan, Australia, and the U.K. Non-U.S. targets made up a record haul of 47%, passing 400 for the first time. Prior to the end-of-year volatility, high valuations in U.S. markets and disruptive forces elsewhere clearly had an impact – as well as swelling activity in Australian and Canadian basic materials industries, only 53% of companies targeted in the Brexit-hit U.K. were targeted by homegrown activists.

M&A activism flourished in a deal-friendly environment: bumpitragage and Elliott Management's take-privates captured the most attention even as the lines between financial and environmental, social, and governance (ESG) activism continued to blur. Activists piling on top of each other at companies like Newell Brands, ThyssenKrupp, Whitbread, and United Technologies highlighted both a limited pool of ideas for well-capitalized funds, and the benefits of incremental pressure as each moved slowly but inexorably in the directions demanded of them.

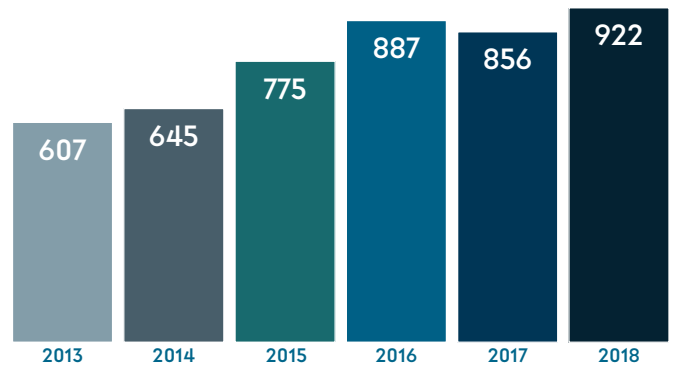
Those tactics meant activists could be effective with smaller pools of capital: according to *Activist Insight Online*, only \$42 billion was invested in new positions in the U.S. and Europe during 2018, compared to \$72 billion the previous year, even as the proportion of targeted companies valued at more than \$10 billion increased.

Activists did not lack for ambition. As we point out in the pages overleaf, they targeted companies with high insider ownership or with no obvious buyer – or both, in the case of Campbell Soup. Triun Partners began a campaign at PPG by calling for the ousting of its CEO, perhaps for the first time.

Yet a year without many big proxy contests meant fewer tests of how institutional investors view activists. Still, activists will have to address the concerns of major shareholders if they are to get a hearing from management teams. As Proxy Insight shows in an article for this report, fears of robo-voting are wide of the mark. Although there has been some talk of engagement-fatigue over the past year, both index funds and active managers are looking deeper into companies for potential risks, with human capital management rising almost to the top of the agenda alongside board diversity.

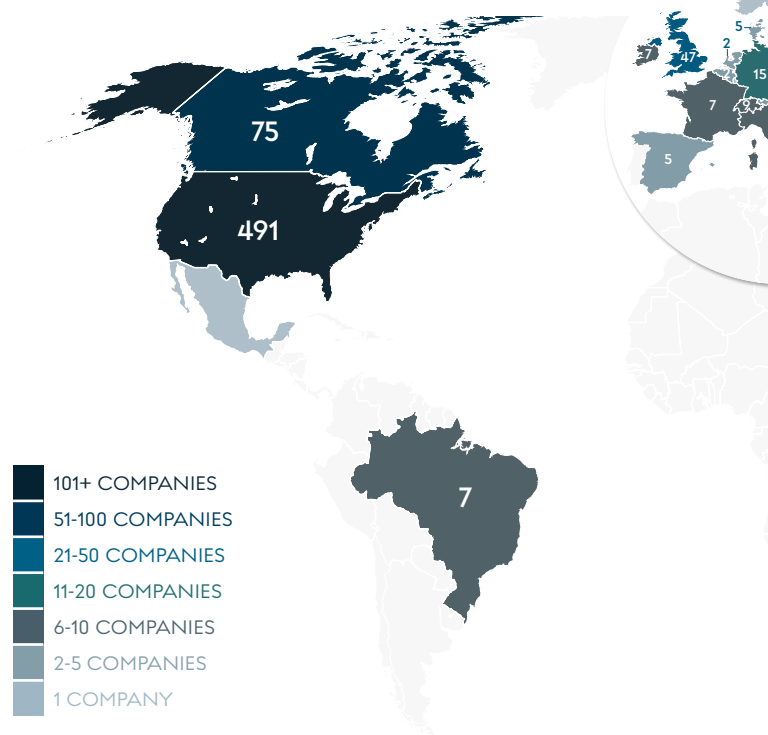
For their support of this report, I am grateful to Georgeson, Innisfree M&A, D.F. King Canada, Alvarez & Marsal, Finsbury, Moelis & Co, and to Schulte Roth & Zabel. It has been a pleasure to put together this report and I hope that our readers find it as enlightening.

## ACTIVIST TARGETS BY YEAR

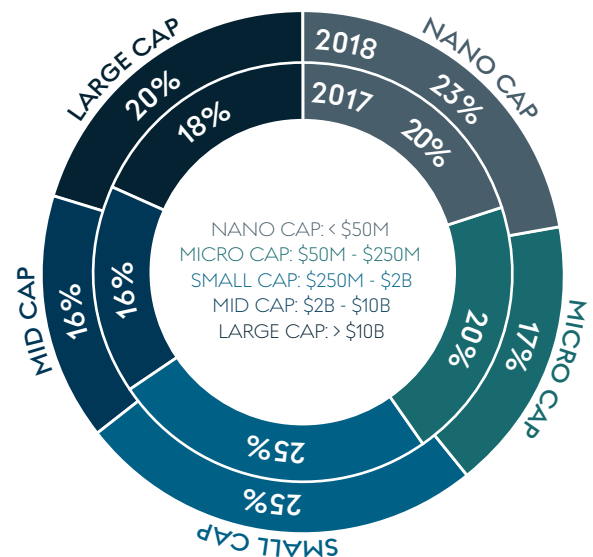


NUMBER OF COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS GLOBALLY, BY YEAR.  
SOURCE: ACTIVIST INSIGHT ONLINE

## ACTIVIST TARGETS BY GEOGRAPHY



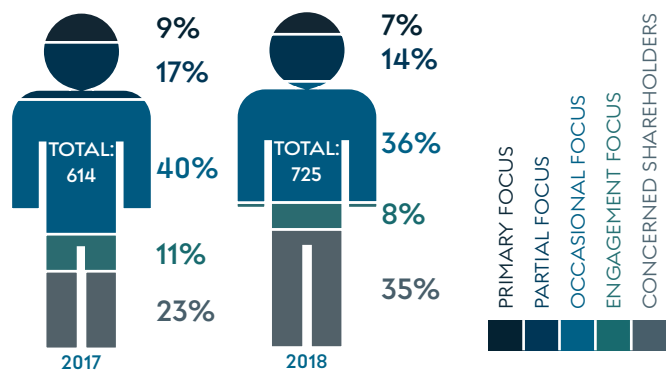
## ACTIVIST TARGETS BY MARKET CAP



MARKET CAP BREAKDOWN OF THE COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS GLOBALLY, IN 2018 AND 2017. NOTE: ROUNDING MAY LEAD TO SUMMATION ERRORS.  
SOURCE: ACTIVIST INSIGHT ONLINE

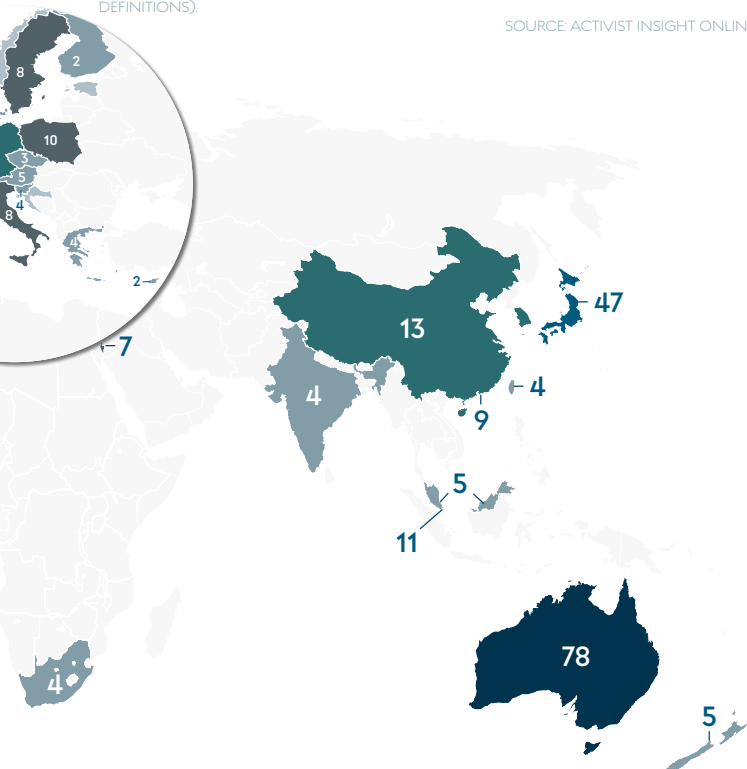


## ACTIVE ACTIVISTS BY YEAR



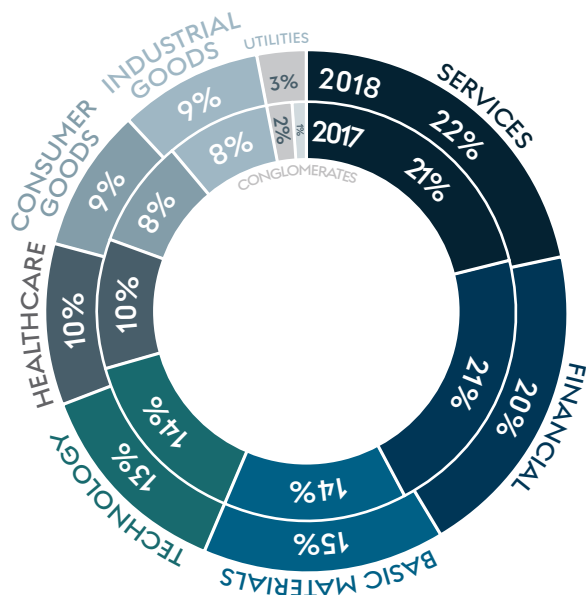
NUMBER OF INVESTORS MAKING PUBLIC DEMANDS OF COMPANIES GLOBALLY, IN 2018 AND 2017, AND A BREAKDOWN OF THOSE INVESTORS BY FOCUS TYPE. (SEE PAGE 4 FOR FULL DEFINITIONS).

SOURCE: ACTIVIST INSIGHT ONLINE



NUMBER OF COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS IN 2018 BY COMPANY HQ. SOURCE: ACTIVIST INSIGHT ONLINE

## ACTIVIST TARGETS BY SECTOR



SECTOR BREAKDOWN OF THE COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS GLOBALLY, IN 2018 AND 2017. NOTE: ROUNDING MAY LEAD TO SUMMATION ERRORS. SOURCE: ACTIVIST INSIGHT ONLINE

## 2019: AN OUTLOOK

Activist Insight predicts household name activists will again struggle to find cause to fight proxy contests, although some campaigns that get stuck on a CEO change or other fundamental disagreement may go the distance.

Although we were wrong about the need for a correction to drive activist activity to record highs, the markets will have an impact on whether the action in 2019 is in the U.S., or overseas. American activists have been studying markets like the U.K., Germany, and Japan for some time and an uptick in activity suggests they are now ready to deploy capital if valuations in the U.S. return to their previous highs. If American markets suffer another rout, however, activists will likely stay home.

ESG did prove to be a consistent theme in 2018, if at a low rumble rather than a continuous roar. That will be the case again in 2019 with some funds racing ahead and others trying to keep up. Expect specialists to be in demand at both activist funds and advisory shops.

Activists may push for transactions at an even more furious pace as credit markets tighten and the outlook begins to darken. Some advisers expect activity to mirror 2008, when overall deal volume fell but hostile takeover attempts boomed. Companies that already have activists on their boards may be especially vulnerable.

Greater urgency may also be injected into operational campaigns as the sugar fix of the December 2017 U.S. tax reform wears off. Expect that to mean CEO tenures and multiyear earnings targets come under scrutiny, with more pressure for transformational changes along the lines seen in 2017.

Private equity's relationship with activism has been an uneasy one for a long time. Some private equity firms, such as Waterton Global Resources, are testing out activist strategies and others are partnering with Elliott Management to acquire companies. Yet others are queasy about being seen as unfriendly to management. "White squire" deals at Avon Products and Hudson's Bay Company are alternative models, though they may not be successful. Whether private equity firms stay on the fence or start deploying dry powder in 2019 may influence strategies across the industry.

Withhold campaigns played an outsized role in 2018, especially for newbie activists that had less experience of advance notice bylaws. Those bylaws may come under greater scrutiny following a 2018 lawsuit at Xerox, setting up another litigious proxy season.

# CHALLENGE ACCEPTED

WHETHER DUE TO LACK OF TARGETS OR SHEER NERVE, ACTIVIST INVESTORS CHALLENGED COMPANIES WITH POWERFUL DEFENSES SUCH AS HIGH INSIDER OWNERSHIP AND DUAL-CLASS STOCK IN 2018. THE TREND WAS PARTICULARLY VISIBLE IN THE U.S., WHERE INSTANCES OF CONTROLLED PUBLIC COMPANIES ARE RARER.

Activists in Europe and Asia have long had to contend with strong and powerful insiders – with mixed results. In 2018, the trend crossed the Atlantic.

Proxy contests at Campbell Soup (41% insider ownership) and Taubman Centers (31% insider voting power) meant that companies with strong protections are no longer shielded from activist attacks. “When you have more difficult targets, I don’t think that necessarily dissuades the activist,” Jason Frankl, leader of FTI Consulting’s activism and M&A solutions practice, said in an interview for this report. “They just need to run a more persuasive and better campaign.”

Frankl believes U.S. activists needed to sail in choppy waters because “the low-hanging fruit has already been approached.”

## SHIFTING TIDE

Activists may have also been emboldened by the growing hostile sentiment toward poor corporate governance and unequal voting rights. Index creator MSCI mulled banning dual-class stocks from its indexes but watered down its proposal by creating new benchmarks that include voting rights in its eligibility criteria.

The likes of index providers BlackRock and State Street generally oppose dual-class structures and staggered boards, with the latter falling rapidly out of fashion. The index providers’ growing clout puts pressure on companies to improve their corporate governance and creates openings for activists in situations they may deem egregious. According to *Activist Insight Governance*, 39 Russell 3000 companies removed classified boards in 2018, up from 24 in 2017.

Controlled companies, defined by *Activist Insight Governance* as firms with more than 50% of voting power controlled by one entity, typically have poorer corporate governance practices than the rest. Only 2% of Russell 3000 controlled firms allow proxy access, versus 21% for Russell 3000 non-controlled companies. Fewer controlled companies have staggered boards than the average, but

such a provision may not be needed when half of the voting stock is controlled by management. As a result, minority shareholders complain they do not have many avenues to hold managements of controlled companies accountable.

## HIGHER HILL

“Stockholders can still engage with controlled entities, you just don’t have much recourse when things go badly,” Jeff Gramm, Bandera Partners’ portfolio manager, said in an interview. Gramm recently lost a proxy contest against restaurant chain Luby’s, which is 39% controlled by insiders. Dissatisfied with the company’s performance, Gramm said, “Luby’s would never have gotten to this point without that high inside ownership and aggressive defense tactics.”

Indeed, activists may need to employ more astute strategies to achieve their goals. In its campaign at Viacom in 2016, SpringOwl Asset Management targeted the executive leadership with a 99-page presentation. Eventually a rift between the company’s top brass and controlling shareholder Shari Redstone drove out the poor performers.

Targeting a controlled entity may also require increased focus, and more resources need to be deployed. “When you have more difficult targets, the activists just need to run a more persuasive and better campaign to convince the management or the board or ultimately other investors that their idea for change is the correct one,” Frankl said.

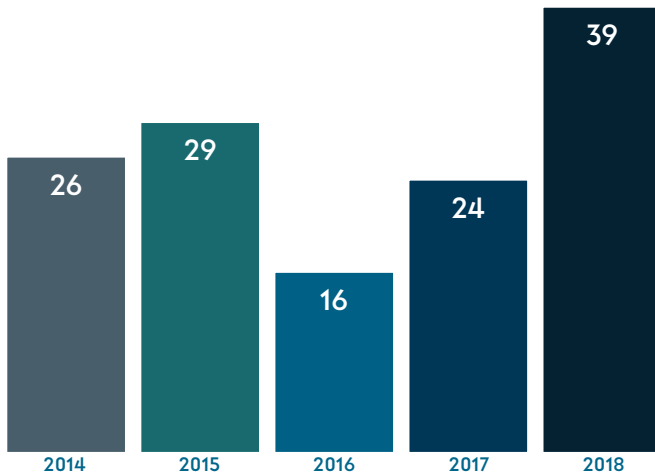
Wholesale changes at these companies is difficult to implement. Third Point Partners was forced to reduce its slate from 12 members to a minority of five at Campbell Soup before settling for three board seats, while Land and Buildings was successful in gaining one seat at Taubman in its second consecutive proxy contest.

Whether activists continue to go after difficult targets depends in no small part on alternatives available in other parts of the market. A correction in stocks could reveal new opportunities. For now, some companies remain de facto out of reach. Their number is dwindling. 📉



“STOCKHOLDERS CAN STILL ENGAGE WITH CONTROLLED ENTITIES, YOU JUST DON'T HAVE MUCH RECOURSE WHEN THINGS GO BADLY.”

## REMOVED STAGGERED BOARDS



NUMBER OF RUSSELL 3000 COMPANIES REMOVING STAGGERED BOARD BY YEAR  
SOURCE: ACTIVIST INSIGHT GOVERNANCE

## MAJORITY VOTING STANDARD

**55.4%**

% OF RUSSELL 3000  
NON-CONTROLLED  
COMPANIES WITH  
MAJORITY VOTING

**18.0%**

% OF RUSSELL  
3000 CONTROLLED  
COMPANIES WITH  
MAJORITY VOTING

DATA AS OF JANUARY 31, 2019  
SOURCE: ACTIVIST INSIGHT GOVERNANCE

## PROXY ACCESS

**21.2%**

% OF RUSSELL 3000  
NON-CONTROLLED  
COMPANIES WITH  
PROXY ACCESS

**2.4%**

% OF RUSSELL  
3000 CONTROLLED  
COMPANIES WITH  
PROXY ACCESS

DATA AS OF JANUARY 31, 2019  
SOURCE: ACTIVIST INSIGHT GOVERNANCE

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# GETTING THE DEAL DONE

2018 SAW A SPIKE IN M&A ACTIVISM AS MORE INVESTORS PUSHED COMPANIES TO GET THE DEAL DONE. ADVISERS ANTICIPATE THE TREND WILL CONTINUE IN 2019 AS THE VOLATILE MARKET CREATES OPPORTUNITIES FOR ACTIVISTS TO PUSH FOR M&A.

2018 was defined by M&A activism, with most of the year's high-profile campaigns involving some sort of deal. Hostile bids attracted vast media attention while bumpitrague tactics continued to provide activists with results. Activists often pushed companies to sell, sometimes disregarding the fact that there was no bidder in sight.

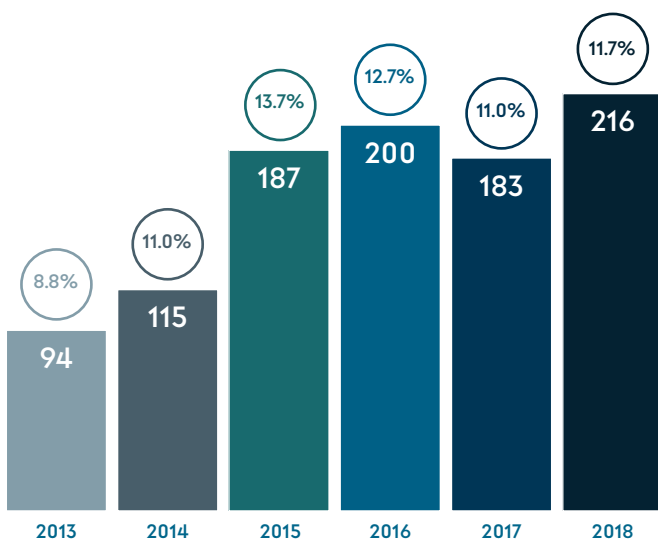
The number of M&A demands increased to 216 worldwide in 2018, up from 183 the previous year, according to data from *Activist Insight Online*. About 67% of demands saw an activist push for a deal while nearly 33% witnessed opposition, proving that most investors are keen to reap the rewards of M&A transactions. Moreover, the number of "push" demands increased 23% year-over-year while "oppose" demands increased 8% in the same period.

Hostile or unsolicited bids continued to present opportunities for activists to push for higher offers, subsequently encouraging takeover targets to accept the updated proposals. "If you don't ask, you don't get," said David Dubner, co-head of Goldman Sachs' activism and shareholder advisory unit, in an interview.

Since 2013, 13 of the 41 U.S. companies facing activist opposition to all-cash bids saw an increased offer price following activist resistance, representing an average jump of 7%, according to *Activist Insight Online*. In 2018, three of six activist-opposed all-cash bids recorded by *Activist Insight Online* received higher offers, averaging an increase of 9%; Carl Icahn and Elliott Management influenced Dell Technologies to increase its bid for VMware's trading stock by 10% in November after the activists expressed opposition to the original offer of \$109 per share. "It's been pretty robust... this has really been the logical time for folks to get involved," added Peter Michelsen, the other co-head of Goldman Sachs' activism unit.

Meanwhile Broadcom and Pebblebrook Hotel Trust both used activist tactics when presenting their hostile bids for Qualcomm and LaSalle Hotel Properties, respectively. Ultimately, Pebblebrook entered a merger agreement with LaSalle, but Broadcom's bid for Qualcomm was shut down on national security grounds. At the same time, Qualcomm faced resistance from Elliott regarding its takeover offer for NXP Semiconductor. The NXP deal was also nixed by

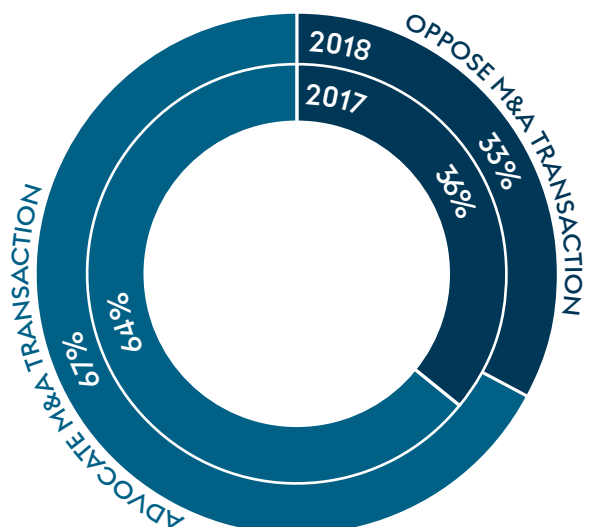
## M&A DEMANDS BY YEAR



NUMBER OF M&A-RELATED ACTIVIST DEMANDS GLOBALLY, BY YEAR, AND SHARE OF ALL ACTIVIST PUBLIC DEMANDS PER YEAR (CIRCLED). (SEE PAGE 4 FOR FULL DEFINITION OF M&A DEMANDS)

SOURCE: ACTIVIST INSIGHT ONLINE

## M&A DEMAND BREAKDOWN



DEMAND-TYPE BREAKDOWN OF ALL PUBLIC M&A-RELATED ACTIVIST DEMANDS MADE GLOBALLY, IN 2018 AND 2017.

SOURCE: ACTIVIST INSIGHT ONLINE



“WITH A LOT OF STOCKS GETTING BEATEN UP, THERE’S CERTAINLY OPPORTUNITY FOR ACTIVISTS TO PUSH COMPANIES FOR M&A ACTIVITY.”

antitrust regulators, signaling a more protectionist climate for dealmakers.

Paul Schulman, managing director and executive vice president at MacKenzie Partners, told Activist Insight that there is a fine balance between pushing for a better deal and scaring the bidder away. “It’s kind of like who blinks first,” he said.

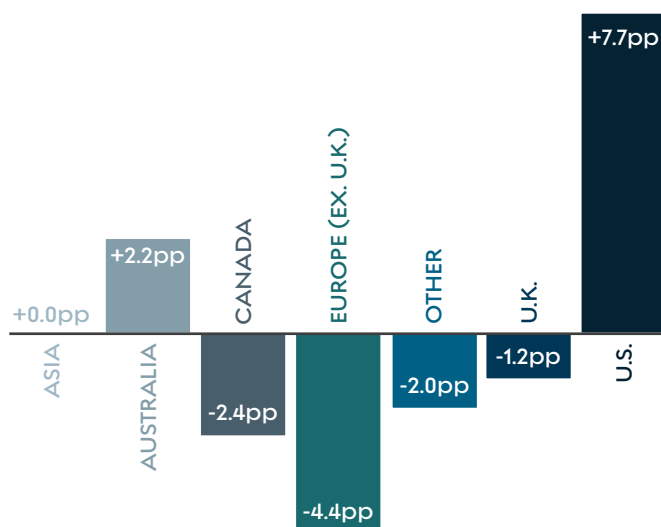
“THIS HAS REALLY BEEN THE LOGICAL TIME FOR FOLKS TO GET INVOLVED.”

2018 also saw several activists pushing companies to sell despite there being no bidder in sight – at both Detour Gold and Campbell Soup, activists Paulson & Co and Third Point Partners went on to win board seats regardless.

Meanwhile, Elliott Management, through private equity arm Evergreen Coast Capital, partnered with Veritas Capital to purchase healthcare software firm athenahealth for \$135 per share in November. The deal came six months after Elliott made an initial bid of \$160 per share, urging then-CEO Jonathan Bush to consider a sale (Bush later resigned). Elliott has already moved on and is bidding for Mitek Systems and QEP Resources. The activist also agreed to acquire Travelport Worldwide alongside Siris Capital Group.

As for the coming year, analysts and advisers anticipate an increase in transactional activism, specifically in the mining and energy industries. As the market becomes more volatile, combinations may become more achievable. “With a lot of stocks getting beaten up, there’s certainly opportunity for activists to push companies for M&A activity,” Schulman concluded. 📌

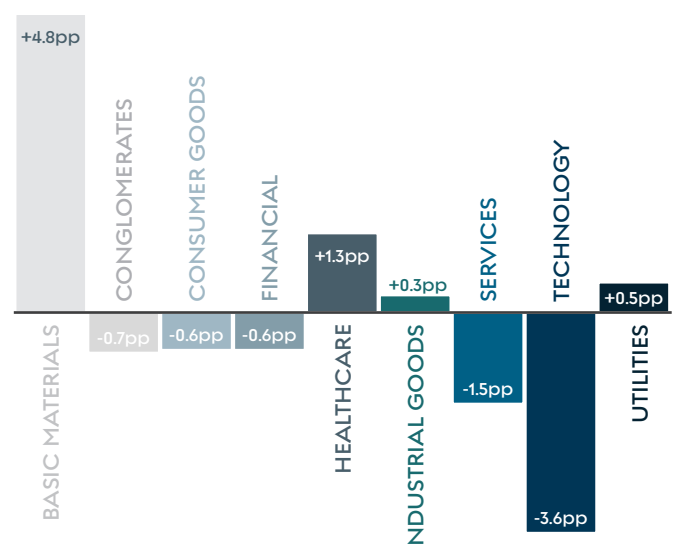
## M&A ACTIVISM CHANGE BY REGION



PERCENTAGE POINT CHANGE BETWEEN 2017 & 2018 OF COMPANIES PUBLICLY SUBJECTED TO M&A-RELATED ACTIVIST DEMANDS BY COMPANY HQ.

SOURCE: ACTIVIST INSIGHT ONLINE

## M&A ACTIVISM CHANGE BY SECTOR



PERCENTAGE POINT CHANGE BETWEEN 2017 & 2018 OF COMPANIES PUBLICLY SUBJECTED TO M&A-RELATED ACTIVIST DEMANDS GLOBALLY, BY SECTOR.

SOURCE: ACTIVIST INSIGHT ONLINE

# TWO NEW FIGHT LETTERS

THE ASSET MANAGEMENT WORLD'S INTEREST IN ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) ISSUES ENTICED ACTIVISTS IN 2018 AND IS SET TO BE THE NEXT BIG THING IN SHAREHOLDER ENGAGEMENT.

In January 2018, when Jana Partners was assailing Apple for the over-exposure of children to iPhones and other devices, Finsbury Senior Adviser Chuck Nathan wrote a blog post questioning whether ESG was genuinely about value-creation, a wedge issue, or a marketing device for activists. "I frankly don't know the answer to that anymore today than when I wrote the article," he said in an interview with Activist Insight for this report.

For all their novelty in mainstream asset management, the first two legs of the ESG tripod took a powerful hold in 2018. Index fund provider Vanguard, historically shy about intervening in the affairs of its portfolio companies, noted in its stewardship report: "A consensus is growing in the investment community that certain environmental, social, and governance matters can significantly affect a public company's long-term financial value." Indeed, it supported one in 20 such proposals during the 2018 proxy season, up from one in 100.

This consensus is due to pressure from asset owners, as well as research by firms that manage capital. Rakhi Kumar, head of ESG Investments and asset stewardship at State Street, told Activist Insight in an interview that the firm's clients are as keen to know how resilient to climate change its portfolios are as her team is of its component issuers. Anne Sheehan, a senior adviser at PJT Partners and former director of corporate governance at the California State Teachers' Retirement System (CalSTRS), which partnered with Jana on its successful Apple campaign, told Activist Insight that support for these campaigns is moving beyond the pension funds that have traditionally pushed for governance changes.

So far, the rising prominence of ESG has mostly led to a plethora of good news stories, with companies ahead in the public relations battle. Asset managers tout successful engagements without airing disagreements publicly. Measurement standards are converging (largely around the Sustainability Accounting Standards Board or SASB) without the need for intervention by the Securities and Exchange Commission, which is more interested in regulating proxy voting advisers than companies. "Who could ever

have imagined that there would be an ice bucket-style sustainability challenge from one CEO to another promoted by the Business Roundtable?" asks governance expert Nell Minnow. "ESG is the fastest growing area of investment and every major financial institution has that option."

While the momentum is likely to carry into 2019, the path may harden for many investors who want to be seen as cutting-edge. From Larry Fink's call for companies to have "a social purpose," issuers are increasingly facing "a paradigm of integrity," says Andrew Behar, CEO of nonprofit shareholder advocacy foundation As You Sow and a critic of asset managers' unwillingness to vote against directors when successful shareholder proposals aren't implemented. Nonetheless, "I'm incredibly optimistic," he says of efforts to make companies more sustainable and stakeholder friendly. "I see the value destruction of those that play by the old rules."

**"WHO COULD EVER HAVE IMAGINED THAT THERE WOULD BE AN ICE BUCKET-STYLE SUSTAINABILITY CHALLENGE FROM ONE CEO TO ANOTHER PROMOTED BY THE BUSINESS ROUNDTABLE?"**

Indeed, for now at least, companies arguably have more to fear from retail investors dumping their stock than from activists buying it. Activists such as Blue Harbour Group and ValueAct Capital Partners, which have either integrated ESG metrics into their main fund's processes or launched impact investment funds, have been the kind that avoid confrontational campaigns. There have been false starts before, including The Humane Society's threat of a proxy contest at Tyson Foods in 2012, when it was reportedly advised by Carl Icahn. "It's always good when investors are supportive of ESG," says Kumar. "We need to see how they demonstrate the commitment they have made." 🐼



“IT’S ALWAYS GOOD WHEN INVESTORS ARE SUPPORTIVE OF ESG ... WE NEED TO SEE HOW THEY DEMONSTRATE THE COMMITMENT THEY HAVE MADE.”

## ESG HIGHLIGHTS IN 2018

### JANUARY 08, 2018

JANA AND CALSTRS URGE GREATER PARENTAL CONTROLS ON APPLE PRODUCTS.

### JANUARY 19, 2018

VALUEACT REPORTEDLY LAUNCHES IMPACT FUND WITH \$100M TARGET.

### APRIL 17, 2018

JANA REPORTEDLY HIRES STAFF FOR ESG FUND LAUNCH.

### MAY 09, 2018

SHAREHOLDER PROPOSAL AT GUNMAKER STURM RUGER PASSES.

### JUNE 05, 2018

JANA APPLAUDS APPLE CHANGES.

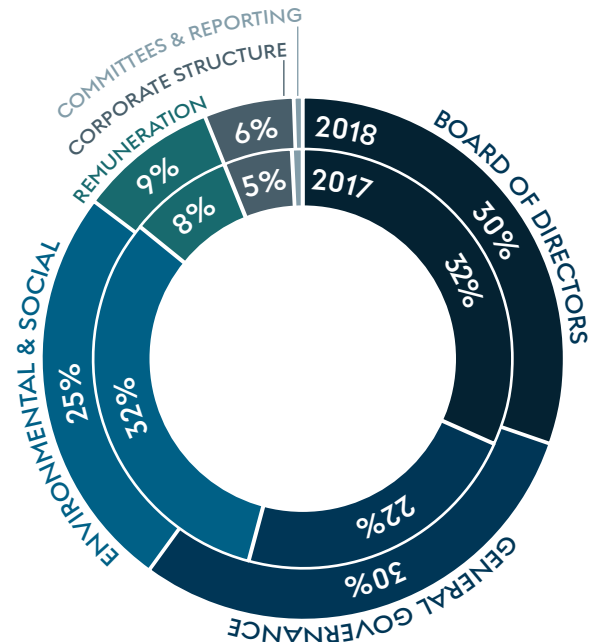
### OCTOBER 01, 2018

PENSION FUNDS PETITION SEC FOR MANDATORY ESG DISCLOSURE.

### DECEMBER 17, 2018

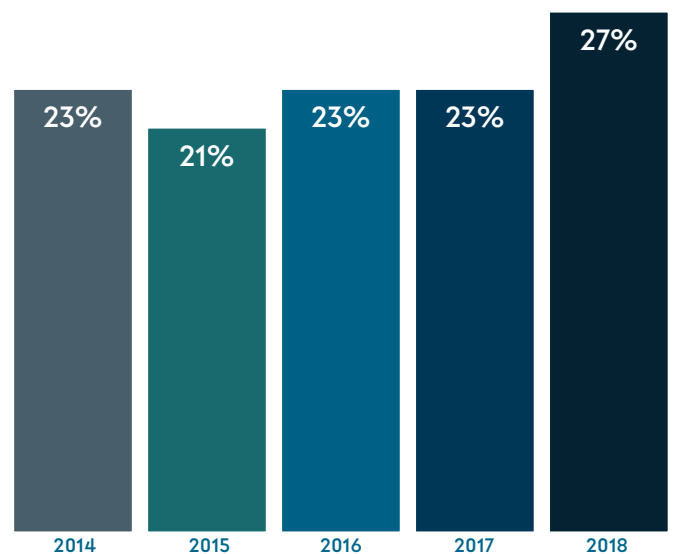
VALUEACT DISCLOSES SEVENTH INVESTMENT IN SPRING FUND.

## INVESTOR PROPOSALS BY CATEGORY



PROPORTION OF SHAREHOLDER PROPOSALS AT COMPANIES WITH A U.S. HQ IN 2018 AND 2017 BY CATEGORY. NOTE: ROUNDING MAY LEAD TO SUMMATION ERRORS.  
SOURCE: PROXY INSIGHT

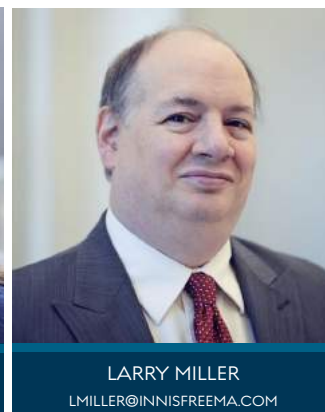
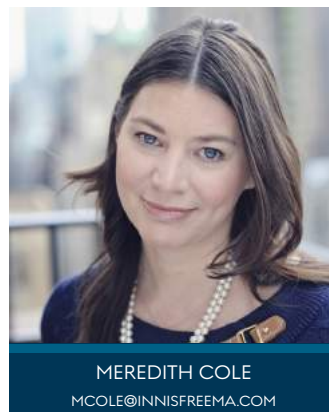
## INVESTOR SUPPORT FOR SOCIAL AND ENVIRONMENTAL PROPOSALS BY YEAR



AVERAGE LEVEL OF VOTES "FOR" ENVIRONMENTAL-FOCUSED SHAREHOLDER PROPOSALS AT COMPANIES WITH A U.S. HQ BY YEAR.  
SOURCE: PROXY INSIGHT

# ACTIVIST DANGER OR PASSIVE PERIL

PASSIVE INVESTING AND ITS IMPLICATIONS FOR SHAREHOLDER ACTIVISM BY MEREDITH COLE, CFA, FOUNDING MANAGING DIRECTOR, AND LARRY MILLER, MANAGING DIRECTOR, OF INNISFREE M&A.



The mutual fund industry has undergone a slow but accelerating transformation over the last 40 years as investors have moved in increasing numbers from actively-managed stock-picking funds to those tied to passive strategies. Cheered for their low costs and easy accessibility for individual investors, passive funds have emerged as a subject of concern for academia, which ponders their impact on corporate governance and potential antitrust issues, and has gone so far as to suggest they should forfeit voting rights.

“[T]HE SUPPORT OF THE MAJOR INDEX FUNDS IS, IN MANY CASES, A POTENTIAL PATHWAY TO VICTORY.”

In *Mad Men* times, a few active managers with good connections could earn 200-300 basis points of superior performance. In the 1980s and 1990s, as markets began to soar, public interest in investing went mainstream – CNBC’s first broadcast was in 1989. In this period, active managers achieved positive results but outperformance was harder to come by. Index funds gained traction – Vanguard managed \$11 million in 1975, when it launched the first index fund; by 1999, its index funds had reached \$100 billion in assets under management (AUM).

With the advent in 2000 of “Reg FD,” which prevents selective disclosure by issuers, and the Great Recession in 2009, active managers struggled to produce enough positive returns to cover their expenses and index funds gained even more traction. In 2014, Vanguard reached \$1.7 trillion in AUM.

This continuing shift in ownership has impacted activism in multiple ways. First, there is a case to be made that the market conditions that have led investors to migrate to the lowest cost providers – enhanced disclosure requirements that have led to a level playing field and a more efficient market – have also led to the establishment of activist investing as a distinct asset class. As the job of beating the market becomes more challenging,

the greater the appeal of an activist strategy that tries not just to prognosticate which stock prices will rise but to drive those returns by advocating changes in companies’ management, operations, financial structure and board composition.

Second, the sheer size of passive holdings can affect a company’s strategy in responding to an activist. Innisfree’s research indicates that the top six index funds including BlackRock, Vanguard, and State Street currently account for (on average) 19% of shares outstanding of the S&P 500 versus 12% for the top nine actively managed funds.

Given the size of investment that the top three index funds now have, it is not uncommon for a proxy solicitor to determine that the outcome of a shareholder vote will be based on how these funds vote. Voting records in proxy contests over the last few years indicate that the largest index funds have supported management nominees at a higher rate than their largest active counterparts. There are no guarantees but gaining the support of the major index funds is, in many cases, a potential pathway to victory.

Finally, the rise in passive ownership, and index investing in particular, has heightened the friction in the marketplace between investors seeking short-term returns and those focused on long-term value creation. Index investors can be viewed as permanent holders of a company’s capital, while active managers, including activists, are paid for outperforming the market, which generally means that they are making shorter-term bets around individual stock performances.

Issuers ignore the short-term at their peril, since subpar stock price returns often give rise to an activist investor entering the stock, and if a settlement is not reached, a proxy contest for director seats. But to win those contests, they must show – to index funds and to all holders – that their boards are composed of directors who take a longer-term view, who are making well-informed and independent decisions about the company’s ongoing strategy and who will monitor and update their own membership to adapt to changing market conditions. 📌

# 2018

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# THE ACTIVIST TOP 10

ELLIOTT MANAGEMENT WINS THE CHAMPIONSHIP BELT FOR THE FOURTH YEAR IN A ROW, WHILE LEGION PARTNERS, VALUEACT, SANDON, AND BARINGTON RETURN TO THE TOP TEN.

Each year Activist Insight creates a ranking of the most influential activists over the past year, based on the number, size, and performance of their activist investments, comprehensively derived from the *Activist Insight Online* database. The following categories have been used to create a points-based ranking of each activist for this year's list: number of companies publicly subjected to activist demands; average market capitalization of targeted companies; success of public demands; average 2018 annualized Total Follower Return\*; and news stories written about the activist on *Activist Insight Online* in 2018. To qualify, an investor must regularly employ an activist strategy and have publicly targeted three or more companies in 2018.

\*Total Follower Return is a calculation of stock price change plus dividends paid from the later of the first close in 2018 or the close on the date an activist's first involvement is disclosed until the sooner of the last close in 2018 or the date an activist discloses that they have exited the position.

## 01. ELLIOTT MANAGEMENT

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	24
AVERAGE TARGET MARKET CAP	\$17.9B
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	-10.3%
ACTIVIST INSIGHT ONLINE NEWS STORIES	351

No activist can compare to Elliott Management's breadth of activity. The omnipresent activist has gone from targeting seven companies in 2013, the first year this review covered, to 24 in 2018 (an improvement of one on 2017) across Asia, Europe, Australasia, and North America. It has claims to be the largest primary or partial focus activist, and a range of strategies that can quickly develop into activism.

Jesse Cohn, Elliott's restless head of equity activism, says the firm is always looking to get better at what it does. "Long ago, there was speculation that activism would die of its own success," he told Activist Insight for this report. "The opposite has proven true."

While 2017 saw the first major deal for Elliott's private equity subsidiary Evergreen Coast Capital, 2018 saw it strike even bigger deals with more established partners Siris Capital and Veritas Capital for Travelport Worldwide and athenahealth, respectively. Already in 2019, it has bid for Mitek Systems and energy company QEP Resources. The option to acquire whole companies has many in the financial world hailing Elliott's flexibility when it engages targets.

With greater influence comes greater scrutiny. Elliott was the subject of lengthy profiles in 2018 obsessed with its reputation for hard-nosed tactics. In a January 2019 letter to the board of eBay, it was at pains to express its "enormous amount of respect for eBay as an organization, for its history, and for the community that comes to work, sell and shop on eBay each day."

Elliott has also gained attention for its development of a team focused on corporate governance, including nominating a four-person board slate with an even gender split at Commvault, which had appointed its only female director just weeks prior, and winning plaudits for its slate at Telecom Italia, where it likely faces another tussle with Vivendi in 2019. "We have a formal strategy tailored to each situation for improving governance at companies we invest in, and we have a team dedicated to it," Cohn adds, although the framework is private for now. "Every company and every board is a little bit different."

While Europe proved a particularly bright spot for Elliott in 2018, with breakups of ThyssenKrupp and Whitbread, Asian markets look harder to crack. It took concessions rather than continuing to oppose the merger of Alps Electric and Alpine Electronics in Japan, and campaigns at South Korea's Hyundai and Samsung are proving a longer slog.

## 02. JANA PARTNERS

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	3
AVERAGE TARGET MARKET CAP	\$253.1B
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	-6.6%
ACTIVIST INSIGHT ONLINE NEWS STORIES	34

Two campaigns summarized Jana Partners' 2018: the traditional, its catalyzing of the \$10.9 billion sale of Pinnacle Foods to Conagra Brands; and the new, a push for Apple to adopt parental controls on its smartphones that set the tone for its development of an impact investing fund. Now, Jana is shuttering its stock-picking funds to focus on activism.

Charles Penner, Jana's partner and the driving force behind Jana Impact Capital, says the fund's focus will be on identifying companies with material environmental and social issues that are weighing on valuation, including customer well-being, human capital management or environmental efficiency. "We're looking at the company first on a bottom-up basis: what's the controversy; what's causing it to be undervalued by the market," he explains.

Scott Ostfeld, co-portfolio manager of activism-only fund Jana Strategic Investment, told Activist Insight the success with Pinnacle followed a string of bets on the consumer retail sector dating back to 2013, including Safeway, PetSmart, Walgreens, ConAgra itself, and Whole Foods Market. "Provided credit markets don't deteriorate further, I think we'll see more public to private transactions," he said of the outlook for 2019.

## 03. CARL ICAHN

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	9
AVERAGE TARGET MARKET CAP	\$11.4B
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	-6.3%
ACTIVIST INSIGHT ONLINE NEWS STORIES	163

Following a slow 2017, Icahn took 2018 by storm. He waged two proxy contests, at SandRidge Energy and Xerox, effectively winning both, pushed Dell to raise an offer for its own tracking stock in a complex transaction that allowed it to tap public markets again five years after going private with only small concessions to Icahn's protestations, and settled with Newell Brands to save the company's CEO, Michael Polk, from facing a full board slate nominated by Starboard Value in another contest. Amid a slew of activist victories, Icahn also saw rival Bill Ackman bow out of a Herbalife Nutrition short position the pair had been on opposite sides of and racked up \$9 billion of asset sales at Icahn Enterprises. The one blemish was a short but abortive effort to prevent the sale of Express Scripts to Cigna.

2019 may see more asset sales, including Navistar, and Icahn is rumored to be playing the casinos in Vegas, albeit by betting stock, not chips.

## 04. STARBOARD VALUE

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	9
AVERAGE TARGET MARKET CAP	\$5.1B
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	11.8%
ACTIVIST INSIGHT ONLINE NEWS STORIES	104

Last year was busy for Starboard Value, which called for change at nine companies in 2018, compared to seven the previous year. The activist successfully pushed for board representation at a handful of companies, often calling for a full board sweep as a tactic to convince the company to settle. Ultimately, Starboard gained 18 seats at six companies, including Mellanox Technologies and Newell Brands. Beyond board changes, the activist successfully pushed for a sale of Envision Healthcare, convinced Cars.com to commence a strategic review, and had its nominee promoted to chief executive at Comscore.

The big question for 2019 will be whether Starboard plans to run proxy contests at its latest investments: Dollar Tree, MGM Resorts, and eBay.



## 05. LEGION PARTNERS ASSET MANAGEMENT

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	7
AVERAGE TARGET MARKET CAP	\$1.6B
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	42.4%
ACTIVIST INSIGHT ONLINE NEWS STORIES	40

Buoyant M&A activity and increased receptivity to activism are the main factors that made 2018 a busy year for Legion, the fund led by Ted White and Chris Kiper. Three of Legion's portfolio companies were acquired in 2018, including Nutrisystem and Nexeo, and the activist placed 12 directors across six companies without launching a single proxy fight. Razor-maker Edgewell Personal Care, Barbie doll manufacturer Mattel, and specialty retailer Genesco are just three companies that settled with the activist.

"It seems that many companies have really become much more receptive to taking feedback from shareholders," White said in an interview for this report. "I think you'll see us place more directors during 2019 than the 12 we placed in 2018, and we view this as a great opportunity to help provide outstanding board talent and other resources to our portfolio companies." The activist is not ruling out a proxy contest in 2019. Legion's only fight to go to a vote thus far was at RCM Technologies in 2013, when it came out victorious.

## 06. THIRD POINT PARTNERS

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	4
AVERAGE TARGET MARKET CAP	\$112.5B
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	-8.5%
ACTIVIST INSIGHT ONLINE NEWS STORIES	81

Dan Loeb's first U.S. proxy contest since 2014 was a doozy, and though Campbell Soup impressively persuaded the members of its founding family – holding 41% of the stock – to circle the wagons, forcing Third Point Partners' to sue and trim its slate, such was the weakness of the company's starting position that it still ended up conceding two board seats.

Third Point continues to make threatening noises at Swiss consumer products giant Nestlé, which is resisting the sale of its stake in L'Oréal, and may yet turn on United Technologies after the estimated restructuring bill for the engineering giant's three-way breakup sent the stock careening downward. A well-timed bet on PayPal, where Third Point prescribed greater cost-discipline and more focused efforts on monetizing its Venmo app, has already paid off.

## 07. SANDON CAPITAL

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	7
AVERAGE TARGET MARKET CAP	\$89.0M
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	27.1%
ACTIVIST INSIGHT ONLINE NEWS STORIES	25

According to *Activist Insight Online*, Sandon targeted seven companies in 2018, up from three in the prior year. The activist lost a vote to wind up closed-end fund Aims Property Securities by a small margin when the manager of the fund voted its shares – a move Sandon contested. Fleetwood finally sold its caravan unit but Sandon's Gabriel Radzynski argues more needs to be done. Elsewhere, Sandon scored success at New Zealand-based Smiths City Group, gaining a seat on the board, and Watpac was sold, albeit below the activist's fair value estimate.

In 2019, Sandon hopes to resolve some of its ongoing campaigns and Radzynski believes Australia will present "phenomenal" opportunities thanks to a combination of "pockets of undervaluation" and a potentially strong M&A market. "The private equity guys will be able to offer significant premiums to the market but even those premiums will be a discount to the true worth of those companies," Radzynski noted.



## 08. ENGINE CAPITAL

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	4
AVERAGE TARGET MARKET CAP	\$461.0M
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	-10.6%
ACTIVIST INSIGHT ONLINE NEWS STORIES	14

Engine Capital saw success at all four companies it targeted in 2018, settling with each firm. The investor convinced Navigant Consulting to enlarge its share buyback plan, and gained four board seats in total at Hill International, Innerworkings, and Team. “Engine looks for undervalued businesses with good balance sheets where there are multiple levers for value creation,” Managing Partner Arnaud Ajdler told Activist Insight, noting that the activist often engages privately before stepping back or increasing pressure depending on the company’s reaction.

Ajdler reveals Engine is currently in discussions with some of its portfolio companies and expects to nominate directors at a number of them. “We certainly can expect more settlements and more board nominations in the near future,” he said.

## 09. BARINGTON CAPITAL GROUP

COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	3
AVERAGE TARGET MARKET CAP	\$862.9M
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	24.2%
ACTIVIST INSIGHT ONLINE NEWS STORIES	17

Barington’s success in 2018 proves constructive and collaborative investing works. The activist seeks to be a long-term investor that provides portfolio companies with plans to maximize shareholder value. In 2018, James Mitarotonda’s firm gained a board seat at embattled cosmetics company Avon Products as well as witnessed the sales of machinery manufacturer Xerium Technologies and plastics firm A. Schulman – the latter 12 years after first buying the stock. The activist is currently undergoing a campaign at restaurants group Bloomin’ Brands, almost a replay of its engagement with Darden Restaurants in 2015.

In 2019, Barington plans to continue employing its strategy at undervalued firms, pushing for improvements in operations, corporate governance, capital allocation, and more. “We believe that the recent decline in the stock market has presented a full pipeline of attractive opportunities,” Mitarotonda told Activist Insight.

## 10. VALUEACT CAPITAL PARTNERS

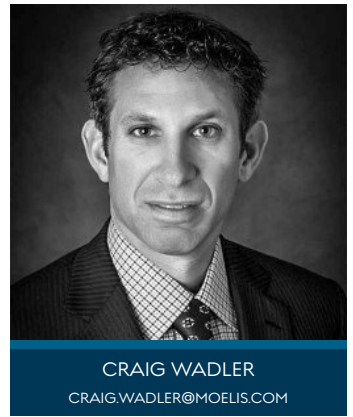
COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS	4
AVERAGE TARGET MARKET CAP	\$8.4B
AVERAGE ANNUALIZED TOTAL FOLLOWER RETURN	-3.3%
ACTIVIST INSIGHT ONLINE NEWS STORIES	31

ValueAct’s most notable moment in 2018 was its branching out into ESG investing with the launch of a new fund. Named ValueAct Spring Fund, the vehicle already made seven investments, including AES, Unifi, and Horizon Discovery Group. It gained board seats at Unifi and AES, while engagements over board representation are ongoing at Horizon and Lindblad Expeditions Group. The activist’s main fund quietly installed board members at Trinity Industries and Seagate Technology.

2019 is already shaping up to be a year of remarkable successes for ValueAct. In a first for a U.S. activist, ValueAct gained representation on the board of Olympus, the Japanese electronics firm that has been plagued by a series of scandals in recent years. In addition, the investor is on track to gain a seat at Citigroup once a conflict of interest is cleared.

# STREET CRED

AN INTERVIEW WITH CRAIG WADLER,  
MANAGING DIRECTOR AT MOELIS & COMPANY  
AND HEAD OF ITS SHAREHOLDER DEFENSE TEAM.



## WHAT WAS BEHIND THE SURGE IN M&A ACTIVISM IN 2018?

Within the activist toolbox, pushing for M&A has always been a preferred way to approach a company – it's an easily understandable strategy that typically delivers the most significant premium, and robust M&A suggests every company has an interested suitor somewhere. 2018 was a terrific M&A environment so an activist's ability to light a flame or throw some kerosene on an existing fire was pretty high.

In terms of bumpitragage, more actively managed funds with large positions are familiar with the M&A process and see nothing to lose by testing that process to get a higher price. A couple of letters, a push from the investment community – it's a logical tool for them to use. Activists make the same calls that they would in a normal campaign but have gained more credibility with this strategy over the last year or so. Companies have been dealing with merger arbitrage forever, but it is now playing out in a more public way.

“ACTIVIST FUND SIZES MAY GO DOWN  
BUT THEIR ABILITY TO RAISE FUNDS FOR  
SPECIFIC CAMPAIGNS COULDN'T BE  
STRONGER.”

## HOW SHOULD A COMPANY DEFEND ITSELF AGAINST CHARGES THAT IT IS NOT PURSUING A STRATEGIC REVIEW WITH ENOUGH VIGOR?

A company's credibility in the market is based on the consistency with which it interacts with shareholders. We advise clients: stick to the plan and communicate with those you need to in order to give them comfort but don't allow them to usurp the process. It's a fine line but it's important to remember how you've interacted in the past with your shareholders. Most serious activists understand the process

by this point; they have sat on boards and understand the way they have to conduct themselves.

## DOES AN ACTIVIST'S ABILITY TO MAKE CREDIBLE TAKEOVER OFFERS FOR TARGET COMPANIES INCREASE ITS EFFECTIVENESS?

Yes, incredibly so. Elliott Management and other similarly-sized activists have been very effective at using their flexibility to create events. The dynamic changes when there are credible buyers at significant premiums. Because of the size and scale of some funds, boards have to react in a way that's more formalized than if the concern is about operations or putting the company up for sale. A company can always reject the bid, but a company has a process it has to go through. My sense is Elliott won't be the only one, because other funds would absolutely want to own 100% of a company at a given price. But that kind of shift wouldn't be entirely new — several well-known activists have made bids for companies in the past.

## HOW WILL VOLATILITY AFFECT ACTIVISM IN 2019?

One view is that, with declining hedge fund performance in 2018, activists will be more on the offensive in 2019 to protect their investment. Also, if certain entry points were unavailable in 2018 but are now reflected in the market, it could be a good environment for new ideas. Stock price is not the only reason a company becomes interesting to an activist, so companies need to be prepared to avoid being caught off-guard.

While it's good for an activist to buy at lower prices there is the potential for redemptions that has to be dealt with. However, a lot of activists are being more creative about raising permanent capital through special purpose and private equity-like vehicles. Activist fund sizes may go down but their ability to raise funds for specific campaigns couldn't be stronger – often on cheaper economics for investors. Activity levels will increase despite assets under management being challenged. 📈

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# ATLAS BUGGED

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BETWEEN COMPANIES AND THEIR SHAREHOLDERS.

For the first time since the beginning of *Activist Insight Online*'s records, over 400 companies were subjected to activist demands outside of the U.S. in 2018, representing a record 47% of all targets. Household names in the activism world branched out into new markets, including France and Japan.

## ASIA

Activism in Asia hit a record high in 2018 with 111 companies publicly subjected to activist demands, compared to 93 in 2017 and 91 in 2016. According to *Activist Insight Online* data, Japan was the focal point, with 47 companies targeted.

An activist that has undertaken multiple campaigns across Asia told *Activist Insight* that while companies were not always welcoming to engagement in 2018, it has been easier to unlock value since Prime Minister Shinzo Abe introduced his namesake capital market reforms. ValueAct Capital Partners also went public with a 5% stake in Japan-based Olympus and in early January 2019, won three board seats.

## EUROPE

In a busy year elsewhere in the activism world, European countries experienced 148 run-ins with activist demands, the only region to see a decrease in activist activity by 6% compared to 2017, according to *Activist Insight Online* data.

Activists took on a number of the big brand names in the U.K. and Europe in 2018, with Third Point Partners at Nestlé and Elliott Management wading into French waters at Pernod Ricard. Elliott also made a last-minute investment in Sky ahead of the eventual auction between Twenty-First Century Fox and Comcast, for which it hired investment bank Greenhill & Co to pitch to the Takeover Panel over a minimum bid price. Mid- and large-cap companies represented 36% of all companies targeted in 2018, only slightly down from 38% in 2017 but a small increase from 35% in 2016.

Engagement opportunities continue to open. Petrus Advisers' Head of Activism Till Hufnagel told *Activist Insight*

that the fund has found it "easier to effectuate change." According to Hufnagel, companies and shareholders in Europe are listening earlier in the engagement, making activists' lives easier. People are learning fast from situations in the U.S., he adds, and are starting to realize that "if a good activist turns up, you should listen."

U.K.-based Whitbread did just that when it sold its Costa Coffee business to Coca-Cola for \$5.1 billion after being pressured to consider a breakup by Sachem Head Capital Management and Elliott.

Elliott also targeted ThyssenKrupp and was successful in pushing out CEO Heinrich Hiesinger. Cevian Capital, meanwhile, openly pushed for a looser conglomerate structure. In September, the engineering behemoth announced plans to split in two by spinning off its capital goods businesses, including elevators and production line construction.

## CANADA

The number of Canadian companies subjected to public demands hit 75 in 2018, a peak since at least 2013, after activity bottomed out at 56 in 2017.



IS L'ORÉAL WORTH IT?

“[IT’S] EASIER TO EFFECTUATE CHANGE AS PEOPLE IN EUROPE LEARN HOW ACTIVISM WORKS.”

Of 2018’s targets, 37% were in the basic materials sector, which enjoyed a brief resurgence before prices again fell in light of a wobbly global growth outlook. The companies targeted include Detour Gold, where Paulson & Co won five seats and removed both CEO Michael Kenyon and Chairman Alex Morrison, and Crescent Point Energy, which survived its first encounter with Cation Capital.

Yet as campaigns at GrowMax and, more recently, Guyana Goldfields highlight, activists may be dependent on lengthy lawsuits and appeals to regulators to enforce their shareholder rights.

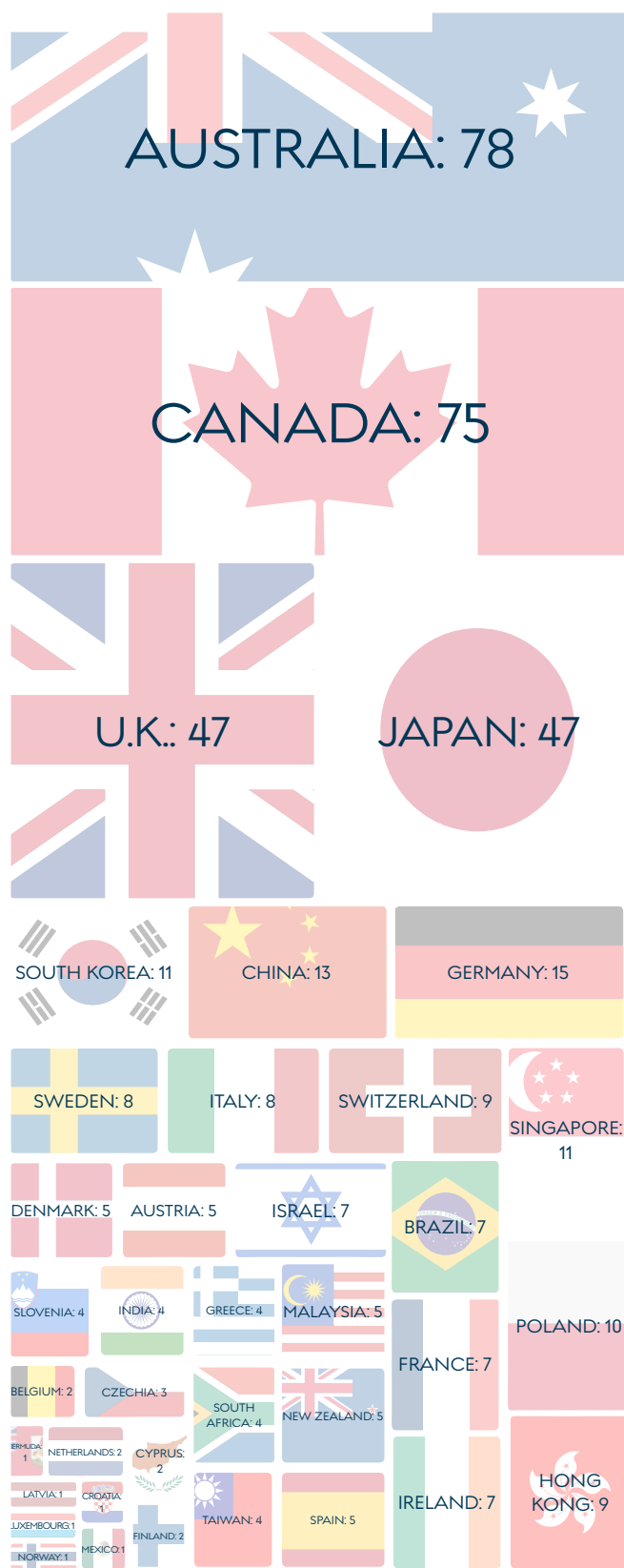
#### AUSTRALASIA

Australia also experienced a record high number of activist engagements in 2018, with 78 companies targeted, up 28% on 2017. Nearly two-thirds of those companies were nano-caps, continuing a historical pattern. In New Zealand, just five companies were subjected to public demands.

Sandon Capital founder, Managing Director Gabriel Radzyminski told Activist Insight the first part of 2018 was difficult for activists, as a bull market made it harder to convince shareholders of the need for changes. “Historically, when markets are tough, investors are more open to different points of view,” Radzyminski said.

The activist also explained that after private equity funds used 2018 for capital raising, they will begin to deploy in 2019. He worries that this will mean shareholders take the first chance to sell out at a cheap price instead of sticking it out for the long run, allowing the funds to buy companies at huge discounts to their intrinsic values.

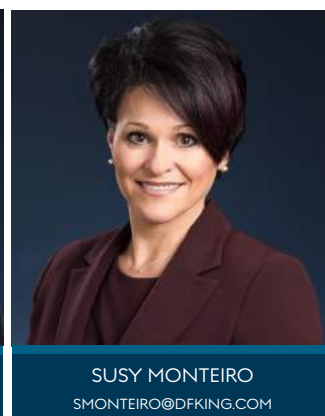
Radzyminski uses Sandon’s situation at Watpac as an example. The activist took a stake and urged the company to sell or divest its mining business and change management. Sandon succeeded in preventing Besix, a 28% stakeholder, from buying 50% of the company’s shares but volatility hit the market and the construction firm made an offer for the whole company that was accepted. “They played their hand well,” Radzyminski reflected. 📌



NUMBER OF COMPANIES PUBLICLY SUBJECTED TO ACTIVIST DEMANDS IN 2018 BY COMPANY HQ. SOURCE: ACTIVIST INSIGHT ONLINE

# BRAND NEW PIQUES

AN INTERVIEW WITH DEXTER JOHN & SUSY MONTEIRO, EXECUTIVE VICE PRESIDENT & SENIOR VICE PRESIDENT OF D.F. KING CANADA.



## WHAT CONTRIBUTED TO THE RECORD LEVELS OF ACTIVISM IN CANADA IN 2018?

**Dexter John:** We believe that the increased level of activism in 2018 has been caused by declining stock prices across the board and, in particular, in the mining/energy sector. That industry has seen hundreds of million dollars of market capital washed away and stocks have seen up to 40-60% declines. Shareholders are very upset when they see that type of decline and the pay structure for management of those issuers going up. Furthermore, we are seeing that investors are upset when they see a lack of alignment amongst the board or management of these issuers that are in decline when the true owners – the shareholders – are feeling all the pain.

“WE BELIEVE THAT OVER THE NEXT TWO-TO-THREE YEARS ESG WILL DISPLACE ‘SAY ON PAY’ AND BOARD DIVERSITY INITIATIVES.”

## WHAT GOVERNANCE ISSUES SHOULD COMPANIES BE AWARE OF GOING INTO 2019?

**DJ:** In 2019, the major governance focus of the likes of Glass Lewis and Institutional Shareholder Services (ISS) will be the harmonization of U.S. and Canadian policies with respect to director overboarding. The one change that was made by ISS was to remove the 75% meeting attendance trigger to only focus on the number of boards the director now sits on.

Something else issuers should be aware of is that ISS is planning to “widen” its scope beyond focusing on S&P/Toronto Stock Exchange Composite issuers, but also on “widely” held issuers based on ISS’ clients’ ownership. The supposed widening of ISS’ scope is very vague and leaves much to discretion. However, as an issuer you still

need to have a woman on the board or at the very least a written diversity policy with measurable goals or targets.

## IS ESG BECOMING AS INFLUENTIAL IN CANADA AS IT IS IN THE U.S.?

**DJ:** ESG is beginning to pick up momentum here in Canada. Back in 2009 ESG was nearly on par with the “say on pay” proposals but for one reason or another it fell off and then board diversity entered the fray. As of late we are beginning to see more ESG proposals being made and a number of large institutions are now amending their own internal guidelines to give guidance on how they will vote based on the issuer’s position on ESG. We believe that over the next two-to-three years ESG will displace “say on pay” and board diversity initiatives unless ISS and/or Glass Lewis intend to broaden the requirements on board diversity and to extend their focus beyond gender.

## HAS THE UNIVERSAL PROXY CAUSED SHAREHOLDER CONFUSION, AS ONE COMPANY WARNED IN 2018?

**Susy Monteiro:** The universal proxy can cause confusion in a contested election. In its current form, the universal proxy is considered a powerful tool to enhance shareholder democracy and corporate accountability because the current proxy system introduces a host of issues such as spoiled ballots, lost votes, confusing vote instruction and what some may call “gaming the system.”

However, where the confusion sets in for investors is when there is a contested meeting and either the dissident or management use the universal proxy instead of both agreeing to use it. When that situation presents itself, the recommendation from ISS or Glass Lewis (who may “split the baby” to have a hybrid board consisting of management and dissident nominees) creates the confusion. The confusion is caused because ISS and Glass Lewis fail to recognize that many institutional holders and most all retail shareholders have no mechanisms to split their vote unless a universal proxy is available. 🇺🇸

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# NEW FLAVORS OF ACTIVISM

AN INTERVIEW WITH MARC WEINGARTEN AND ELE KLEIN, CO-CHAIRS OF SCHULTE ROTH & ZABEL'S GLOBAL SHAREHOLDER ACTIVISM GROUP.

ACTIVISM HAS GROWN AS MARKETS HAVE TRENDED SMOOTHLY UPWARD. WILL VOLATILITY PUT OFF SOME OF THE NEWER ENTRANTS?

**Marc Weingarten:** I don't think so. I've always had some concern that substantially rising markets would lead to a reduction in activism by just kicking the number of targets out of price range, but I've been proven wrong. There are always relative underperformers in generally rising markets, and the activists have seemed to manage to find targets in rising markets and falling markets. I don't think the volatility has deterred new entrants or existing participants.

DO YOU EXPECT ACTIVISM AS A TOOL TO CONTINUE CATCHING ON WITH SOME OF THE LESS TRADITIONAL ASSET MANAGERS?

**MW:** I think non-dedicated activists will increasingly try activism when they're stuck in a position they are not happy with. I think they're going to continue to try their hand. We've had many clients on that basis. Some of them had to be educated that activism was not as easy as it looked, but I think they will increasingly be trying it.

The quant funds, the major institutional investors – I'm not so sure. I think they will engage with their portfolio companies increasingly, but I don't see them as very likely going full-blown into activism looking for board seats or waging proxy contests.

**Ele Klein:** I've seen the exact same thing Marc is saying on these institutions and the index type of investors. They are bulking up. They're taking it much more seriously in terms of figuring out what they want, but they seem to be primarily bulking up to be able to deal with the situations and to deal with them on their own.

M&A ACTIVISM HAS BEEN MORE PROMINENT THAN MASSIVE PROXY FIGHTS. DO YOU SEE THAT CONTINUING?

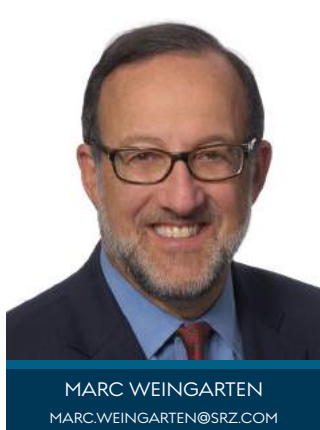
**EK:** M&A activism is going to be a big part of the market, at least as long as the M&A market stays healthy. Obviously, if there is a shift or a downturn in the economy, that can have a change in all M&A activity, and M&A activism will go along with that.

There are a lot of deals out there. Therefore, there's a lot of scrutiny and a lot of criticism of pricing that's taking place on one hand. The flipside of that is people are seeing a frothy market, and it's an opportunity. It's a time to drive change and to take advantage of what may be high prices that we may not see for much longer. So there's pressure on both sides of the equation to get things done.

And what's fascinating is the actual participation in the M&A landscape. Elliott has done this very successfully on a number of campaigns, partnering with other firms and saying, 'Look, we will tell you to sell yourself, but we will drive that change if you don't think that's the right answer.'

ANOTHER BIG THEME IN 2018 WAS ESG ACTIVISM. DID IT SURPRISE YOU HOW BIG A PART IT PLAYED, AND DO YOU EXPECT TO SEE IT EXPAND?

**MW:** It certainly got a lot of press. I'm not sure there have been all that many ESG-predominant activist campaigns. I don't get it. I always question really whether this is more lip service than reality, because the activists are all hedge funds and they're trying to maximize shareholder value. I query whether ESG is really going to get them there and whether it's going to get them there in the near term. But it's certainly the flavor of the month.



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EK: I'm a little more optimistic but equally cautious. I think that you have certain dedicated funds, and, obviously, it's about returns. And I think they're feeling themselves out in how to drive those returns through the ESG platform. I'm more optimistic in the sense that I think they will figure something out.

#### WHAT WAS THE WORST ENTRENCHMENT DEVICE YOU SAW IN 2018?

EK: Roaring Blue Lion and HomeStreet – that was an example of figuring out a way to survive a campaign with no shame, figuring out a way to not have to be responsive to the shareholders' will. That's a pretty egregious example, and the story is not fully written there yet.

MW: In many cases, the nomination notice requirements and bylaws have gone way over the top. I don't think, at least in Delaware, that those provisions will be upheld.

EK: We're involved in another flavor where the adoption of certain poison pills with broad language about acting in

concert and things like that sort of leaked into the space. Even quality defense firms would say that they're not sure that those flavors aren't a breach of fiduciary duty. But other people push for them, and when you start pushing back as Icahn did at SandRidge, companies tend to run for the hills.

#### IS THIS A TURNING POINT FOR ACTIVISTS TO BE TRULY GLOBAL IN HOW THEY APPROACH THEIR PORTFOLIOS, OR ARE VALUATIONS DRIVING OVERSEAS ACTIVISM?

MW: I do think it's a continuing trend. There will be increasing levels of activism abroad. It is in part due to how robust the U.S. economy and stock markets are. Activists see more value abroad than in the U.S. markets generally. It takes a fair amount of infrastructure for activists to do a foreign campaign. It's a whole different skillset that only the largest activists have attempted.

EK: You have the U.S. people going across the waters – that may be more of a challenge – but there are startups that are just concentrating on individual areas like Asian-dedicated activists and you're going to see more of that.

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## AN INTERVIEW WITH ANELIYA CRAWFORD, PARTNER IN THE SHAREHOLDER ACTIVISM GROUP.

#### SETTLEMENTS ARE ON THE RISE, BUT ARE NEGOTIATIONS OVER THEIR TERMS BECOMING MORE HARD-FOUGHT?

Aneliya Crawford: Yes, the deals that companies and activists strike have become more nuanced. A settlement must ensure that the change needed will be made or, at the very least, the company is positioned to tackle the issues. This means agreements must be tailored to provide for the best selection process for agreed-upon directorships, committees must be formed and empowered to oversee strategic reviews, the return of the activist has to be contemplated under certain circumstances, and many other situation-specific factors and needs must be addressed.

Finding the optimal structure of cooperation between an activist and the company is further complicated by the expectations of increasingly engaged institutional investors.

#### ARE CEOs NOW LESS LIKELY TO BE THE TARGET OF A CAMPAIGN?

AC: I don't think so. There was a peak of high-profile CEO activism a couple of years ago, followed by 2018's greater focus on M&A and governance issues. But that is not to

say there is no room for operational activism. At its core, operational activism is an evaluation of the performance of a CEO, whether the CEO's head is one of the formal demands or not.

#### DO YOU ANTICIPATE A BUSY YEAR IN 2019?

AC: Yes, I do. The opportunities are there, and traditional, well-capitalized activist funds as well as disgruntled shareholders willing to start their first fight are ready to roll up their sleeves. All indications are for a busy 2019. 🙌



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# THE FRONT LINE



INTERVIEWS WITH MICHAEL SWARTZ, CO-CHAIR OF SCHULTE ROTH & ZABEL'S LITIGATION GROUP AND HEAD OF ITS SHAREHOLDER ACTIVISM LITIGATION PRACTICE, AND JIM MCNALLY, LONDON-BASED PARTNER IN SCHULTE ROTH & ZABEL'S GLOBAL SHAREHOLDER ACTIVISM GROUP.



## HOW DO YOU SEE THE PLX DECISION AFFECTING ACTIVIST M&A CAMPAIGNS GOING FORWARD?

**Michael Swartz:** Overall, I would resist the temptation to draw too much from the PLX decision from an activist perspective. Less than two years ago, the same Delaware Chancery Court judge granted a temporary restraining order on behalf of our client, venBio, blocking biopharma company Immunomedics from entering into a worldwide licensing agreement for its only viable product. There, venBio's thorough and well-reasoned proxy campaign factored favorably in the court's analysis, notwithstanding the company's attempt to portray venBio as a short-term activist.

Accordingly, these types of cases are highly fact-dependent. Activists definitely need to be aware that courts will take account of their plans and proposals when reaching decisions, and some will even be biased against them, which can impact the court's perspective and decision. Activists need to be particularly vigilant when serving as board members because their actions may be subject to enhanced scrutiny, particularly in light of the campaign they pursued to get elected.

## THERE SEEMS TO BE MORE LITIGATION AROUND DIRECTOR NOMINATIONS. WHAT SHOULD ACTIVISTS BE AWARE OF?

**MS:** Companies are beginning to "litigate" shareholder-proposed director nominations ahead of time by bolstering their advance notice bylaws and requiring absolute fidelity to them. The HomeStreet case from 2018 provides the perfect example of this phenomenon. HomeStreet was successful in rebutting an activist's notice letter, and thus its director nominations, on purely technical grounds – failure to satisfy certain mechanical details set forth in the company's advance notice bylaws. A Washington state court sided with the company and held the nomination notice to be invalid.

## ACTIVISTS HAVE BEEN SURPRISINGLY SUCCESSFUL IN EUROPE IN 2018. IS THIS A TURNING POINT?

**Jim McNally:** There has certainly been opportunity, and the markets (in the U.K. particularly) have been volatile by historic standards. Activists are getting more traction in Europe with targets and their boards and are now more likely to get the sympathetic ear of institutional investors and the financial press. This has helped open up additional European markets for activism where perhaps there has been less of a culture of direct shareholder engagement and, consequently, where there are still untapped opportunities.

That said, there are still hurdles to pass for activists, particularly when running campaigns in those jurisdictions where the legal framework is less supportive of direct investor engagement, such as those with dual board structures.

## THE WEAK POUND HAS BEEN GOOD FOR ACTIVISM AND M&A IN 2018 – WILL THAT CONTINUE?

**JM:** Sterling has been depressed largely as a result of Brexit uncertainty and the impact that has had and is having on the U.K. economy. Whilst the effect of Brexit remains uncertain and the manner of Brexit remains unclear, the downward pressure will likely continue. Whether this presents a short-term opportunity for activists and buyers in the U.K. market or a longer-term fetter on U.K. growth and prospects remains to be seen.

In 2018, some sectors have had new hurdles for M&A activity – new U.K. rules introduced in the summer are more protective of businesses relating to military and dual-use technology, computing hardware and quantum technology. 📌



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# SHAKY GROUND, SHAKY PERFORMANCE

AN UNSTABLE GEOPOLITICAL CLIMATE CONTRIBUTED TO POOR RETURNS FOR ACTIVIST INVESTORS IN 2018. AND WHILE ANALYSTS PREDICT CONTINUED VOLATILITY FOR THE MARKETS, THEY BELIEVE ACTIVIST RETURNS WILL IMPROVE IN THE YEAR TO COME.

Unstable political climates in countries including the U.S. and U.K. caused tremendous uncertainty for global markets in 2018, with activists feeling the brunt thanks to their concentrated portfolios. Specifically, increased interest rates, trade wars, and Brexit dented investor confidence in the global economy. “The market needs stability in the ecosystem that it operates in to perform well,” said Ali Dibadj, a partner at investment management and research firm AllianceBernstein.

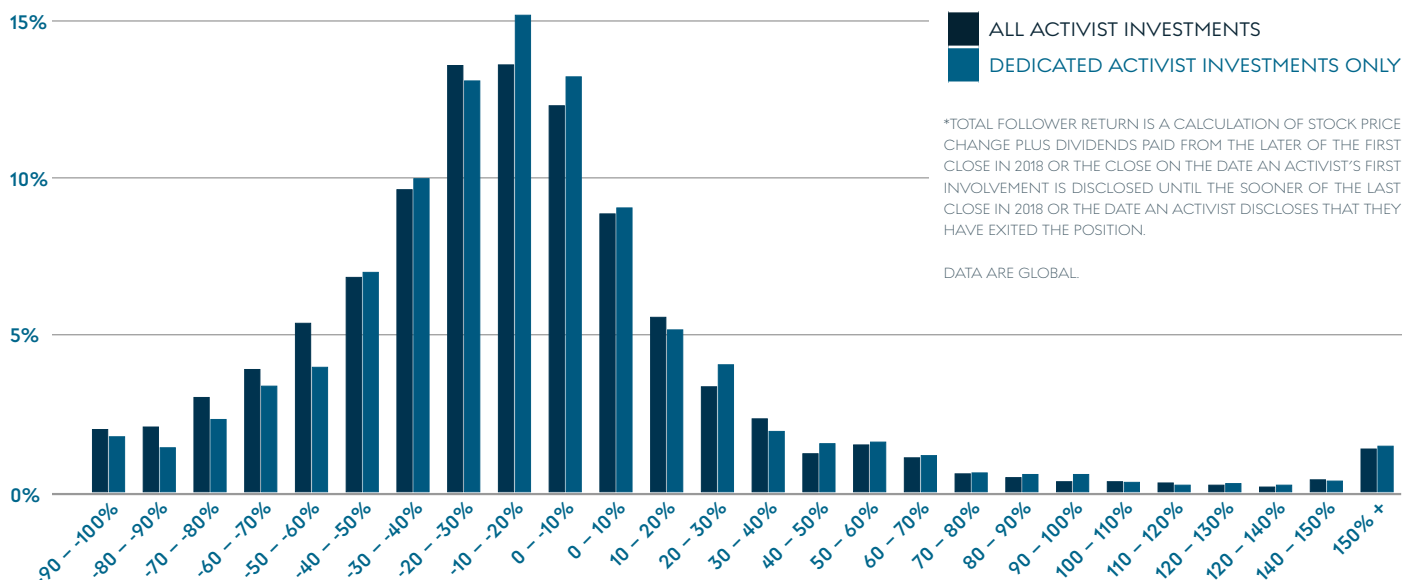
The S&P 500, MSCI World, and Activist Insight indexes performed significantly worse in 2018 than in previous years. The Activist Insight Index had returned 7.6% net of fees by the end of the third quarter of 2018 – the latest period for which full results were available – 345 basis points lower than during the same period in 2017. Meanwhile, the MSCI World Index slipped to 5.9% and the S&P 500 Index dropped to 10.6% during the same period. By the end of 2018, the S&P 500 produced a total return of negative 4.4%, a reflection of the fourth quarter’s reversal of positive returns seen during most of the year.

Many well-known activist hedge funds ended 2018 in the red. Dan Loeb’s Third Point Partners’ public fund lost 10.6% while Bill Ackman’s Pershing Square Holdings was down 0.7% after fees. In addition, David Einhorn’s Greenlight Capital reportedly declined 34%, its worst performance since inception in 1996.

A tougher climate for fundraising that began a couple of years ago is growing chillier by the day. “I would suspect overall assets have gone down and not just because of performance but also investor redemptions,” Marcos Veremis, a managing director at Cambridge Associates, said, suggesting that investors are losing faith in the activists they support.

“THE MARKET NEEDS STABILITY IN THE ECOSYSTEM THAT IT OPERATES IN TO PERFORM WELL.”

## ANNUALIZED TOTAL FOLLOWER RETURNS\* (%) OF ACTIVIST INVESTMENTS IN 2018



SOURCE: ACTIVIST INSIGHT ONLINE

“I WOULD SUSPECT OVERALL ASSETS HAVE GONE DOWN AND NOT JUST BECAUSE OF PERFORMANCE BUT ALSO INVESTOR REDEMPTIONS.”

According to *Activist Insight Online*'s follower returns stocktracking feature, the median annualized total follower return from an activist-owned stock was negative 17.1% in 2018 – lagging the S&P 500 Index. Funds with a dedicated activist strategy did slightly better, returning a median annualized negative 15.1%. In addition, approximately 28.9% of dedicated activist targeted stocks saw a positive total annualized return in 2018.

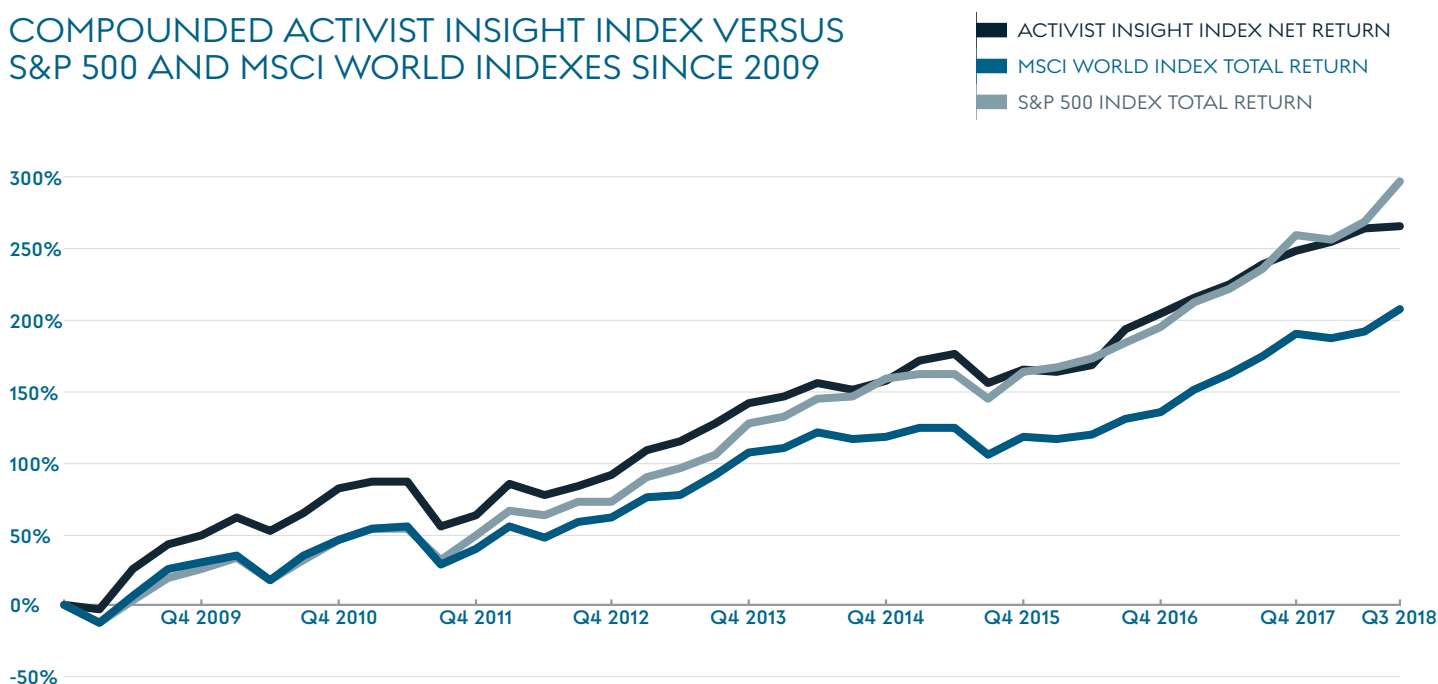
Dedicated activists performed relatively well in sectors like healthcare and technology, achieving positive returns in 37.1% and 36.5% of investments throughout 2018 respectively. Meanwhile, the industrial goods and consumer goods sectors were not as stable, causing activists to suffer from investments in “under pressure” companies that have not performed well over the past year. Meanwhile, companies with a market-cap over \$2 billion performed better than those under \$2 billion, with 34.6% and 26.4% of the stocks respectively, achieving a positive return throughout 2018.

Moving forward, Dibadj predicted the markets will continue to be volatile in 2019. Strategy was the most influential indicator of a successful activist investment, Dibadj said, noting that operational activists performed better than those that adopted a balance sheet or fire sale strategy despite General Electric's continued slide, which left it down 58% by year-end. “The most successful activists really consulted with management teams and really understood the business,” he said.

Dibadj said he believes 2018's poor performance will not affect activists in the long run. “A lot of what good activists do is long-term in nature so if their strategy is correct, one year shouldn't matter,” he pointed out.

Veremis went further, noting that with 2019 likely to produce a difficult environment for the markets, activists could take advantage. “If we move toward a recession, that's when activists will have an opportunity to enter companies on the cheap, make changes, and leverage that period to make returns,” he said. 📈

## COMPOUNDED ACTIVIST INSIGHT INDEX VERSUS S&P 500 AND MSCI WORLD INDEXES SINCE 2009



# ONE RULE TO RULE THEM ALL

AN ARTICLE BY CAS SYDOROWITZ,  
GLOBAL HEAD OF ACTIVISM AT GEORGESON.



Facing an activist investor is no easy feat for any management team, particularly because every campaign is different. These guidelines provide a starting point for thinking about an engagement that will keep you out of hot water.

## RULE NO. 1: THERE ARE NO RULES

When it comes to activism there are no standards and dealing with an activist can be very challenging and time-consuming when you are trying to run a business. However, there are things that companies should consider when they find an activist as one of their shareholders.

**JOIN FORCES:** Assemble the defence team – including your legal counsel, your PR team and your shareholder engagement firm (proxy solicitor).

**KNOW YOUR ENEMY:** Identify the activist and the types of campaigns they have run previously – no two activists are alike. Look at their demands in a critical, unemotional light. What is the source of the inputs for their thesis and what time period does it cover, i.e. is the period chosen specifically to make the results look worse than they are? What does success look like for the activist? Consider how they get paid – 2% of assets under management and 20% of the return for the specific investment? The second fee provides more clues about what they really want to achieve.

**GET CLARITY:** What percentage of your shareholder base has been identified? How much is in actively managed accounts versus passive ones, and how much is in retail versus institutional shareholdings? Do employees or directors own a significant portion of your shares? Identify the other stakeholders that have a voice, including employees, unions, pension trustees, debt holders, regulators, local or federal government.

**LOOK BACK:** Take an inventory of your shareholders, when you last met them, and what their views were. How did those same shareholders vote at your last shareholder meeting? How did the proxy voting advisers recommend at

your previous meetings? Any against recommendations will be picked through by the activists.

**QUESTION YOURSELF:** Has the company's strategy and priorities been clearly articulated to the market? Repeat the strategy and those priorities after re-reading the activist communications; what are they missing, or what is the company lagging on delivering? Also, are there any skeletons in the closet? Be truthful within the boardroom, as you do not want anything coming out in the press which will hinder the defence campaign.

“PARTICULARLY BECAUSE AN  
ACTIVIST SITUATION IS HARDLY EVER  
PREDICTABLE, COMPANIES SHOULD BE  
PREPARED AT ANY TIME.”

**GET READY:** Define the internal teams who will take ownership for the different work-streams, refuse to hold all-party calls, get the owners of the various work-streams to document in three bullet points or fewer the key developments and changes for the senior defence team.

Particularly because an activist situation is hardly ever predictable, companies should be prepared at any time. Having an experienced adviser such as Georgeson at your side throughout the year will help you alleviate the effects of an unexpected situation. Only highly-specialised advisers can anticipate how shareholders will react to different scenarios and know what drives their decision process as they are the ones dealing with the governance community. Your shareholders are resource-constrained so they may not be readily available to speak/meet with you. Your advisers will navigate how to get an audience with the right contact. 📞

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# SETTLING THEIR DIFFERENCES

SETTLEMENTS FOR BOARD SEATS WERE ON THE RISE IN 2018, INDICATING BOTH A GROWING ACCEPTANCE OF SHAREHOLDER ACTIVISM AND THE RETURN OF THE AMICABLE RESOLUTION.

The number of settlements increased strikingly in the U.S. in 2018, showing a preference for companies and activists to nip hostilities in the bud. As a proportion of all demands for board seats, agreements reached a four-year high at 71% of the total.

142 U.S. settlements were recorded in 2018, versus 119 in 2017 and 168 the year before. Only 23 demands for board seats went to a shareholder vote in 2018, down from 26 in 2017 and 25 the previous year.

Including the U.S., 207 settlements were inked globally in 2018, representing more than half of total board representation demands. In Asia and Continental Europe, areas historically deemed unfriendly to activism, most engagements went to a vote. Elliott Management won a remarkable victory for a majority of the board at Telecom Italia in a highly-publicized fight against the largest shareholder, Vivendi. Elliott launched two campaigns for board seats in 2018 in Europe, behind Amber Capital, which launched four board campaigns.

Although the number of board actions in Asia dropped, the number of seats won via settlements doubled to 16. Usual

suspect Oasis Management and South Korea-based Value Partners Asset Management were the busiest activists in Asia for board campaigns.

In Australia and the U.K., the number of settlements increased both on an absolute basis and as a proportion of total board representation demands, although they remain well below U.S. levels. In Canada, which saw one of the biggest proxy fights in 2018 at Detour Gold, agreements rose at a slower rate than total board representation demands.

## WHOLESOME SOUP

The rise in U.S. settlements may not be a big surprise, given that companies and investors have historically sought to avoid proxy contests since activism became mainstream. Marked by a few battles that went all the way to a vote, such as Procter & Gamble versus Nelson Peltz's Triun Partners and Pershing Square Capital Management against Automatic Data Processing, 2017 may have been a distinctive year. 2018's biggest fight, Campbell Soup against Third Point Partners, ended in a settlement.

"2017 was somewhat of a unique year in the sense that we saw several high-profile proxy contests go to a vote, which is not the norm," David Whissel, executive vice president at MacKenzie Partners, said in an interview. "The increase in settlements in 2018 was more likely a reversion to the mean."

## ASSERTIVE VERSUS CONSTRUCTIVE

Yet the increase could also signify that companies are more willing to entertain activist proposals, particularly if they are reasonable, according to Michael Verrechia, a managing director at Morrow Sodali. Activists such as ValueAct Capital Partners and Legion Partners Asset Management have long been known for advancing demands for one or two seats at most, something that most boards are willing to consider. Indeed, Legion was prolific in 2018, installing a total of 12 directors at six companies. ValueAct inked settlement agreements for one seat with four companies.



PAST ITS SELL-BY DATE.

“WE ARE CONCERNED THAT SETTLEMENTS IN GENERAL ARE SHORT TERM AND ACCOMMODATE THE DEMANDS OF ONE SHAREHOLDER WITHOUT PUBLIC DEBATE.”

Such engagements typically stay below the radar until a settlement is announced. More aggressive activists such as Carl Icahn and Starboard Value gained more seats, but their successes were preceded by public antagonism or proxy contests. Icahn won 15 board seats at four companies in 2018, including board majorities at Xerox and SandRidge Energy following proxy contests. Meanwhile, Starboard installed as many as 18 directors at six issuers.

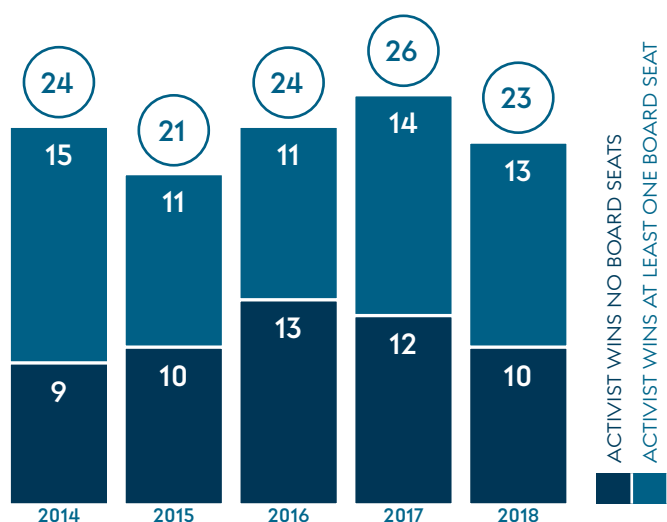
### CONCERNED SHAREHOLDERS

Settlements may not be such good news for other shareholders, including institutional investors that may prefer to have a say over the composition of the board. “We are concerned that settlements in general are short term and accommodate the demands of one shareholder without public debate while resulting in governance and strategic changes that impact the long term,” Matthew DiGuiseppe, a vice president at State Street’s Asset Stewardship division, said in an email. Similar concerns were raised in recent years by the likes of BlackRock and Norway’s pension fund, among others.

In the past, State Street called on both activists and companies to consider long-term interests in the settlement process, including by increasing the duration of the agreements and adding limits on selling or pledging shares. DiGuiseppe said he had yet to see progress in that area, although he admitted that communication with shareholders has improved. “In activist situations we want long-term shareholders’ perspectives to be considered regardless of the outcome being a settlement or proxy vote,” DiGuiseppe said.

That said, since proxy contests are expensive and divert management’s attention from operations, some shareholders favor a swift resolution, albeit not without prior consultation with the broader shareholder base. “Shareholder engagement is critical at all times, but particularly when a company is dealing with a shareholder activist,” Whissel said. “Ideally, the decision of whether or not to settle reflects investor perspectives as well as the board’s assessment of what is best for the company.”

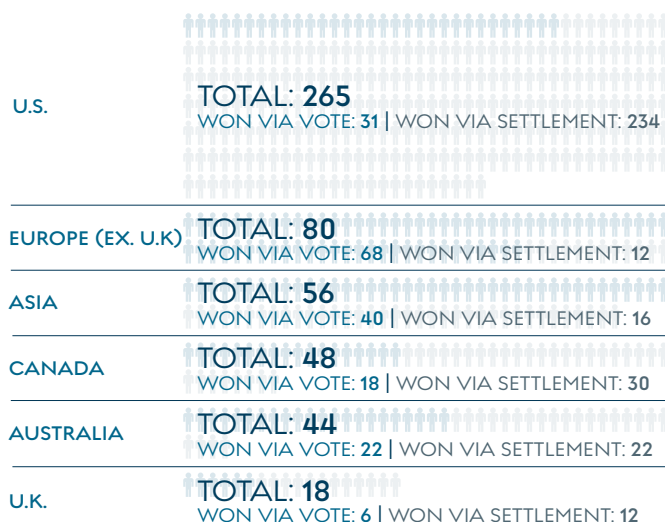
## PROXY CONTEST VOTE OUTCOMES



NUMBER OF PROXY CONTESTS THAT WENT TO A VOTE AT COMPANIES WITH A U.S. HQ BY YEAR (CIRCLED) AND EVENTUAL OUTCOME.

SOURCE: ACTIVIST INSIGHT ONLINE

## ACTIVIST BOARD SEATS GAINED IN 2018



NUMBER OF BOARD SEATS GAINED BY ACTIVIST NOMINEES BY COMPANY HQ, AND METHOD OF FULFILLMENT.

SOURCE: ACTIVIST INSIGHT ONLINE

# THE THIN END OF THE WEDGE

ACTIVISTS' ADOPTION OF ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) ISSUES SHOW THEIR ABILITY TO ADAPT TO SUCCEED. AN ARTICLE BY FINSBURY'S PHILIP WALTERS, MANAGING DIRECTOR, LONDON; KAL GOLDBERG, PARTNER, NEW YORK; AND HERING SCHUPPENER'S JOBST HONIG, DIRECTOR, BERLIN.

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For many, activist investors embracing socially responsible investing is a contradiction in terms. The consummate corporate raider, they argue, sees ESG as nothing more than a campaign wedge issue to garner support from institutions. It is another angle for activists to exploit to help them succeed.

Activists, however, argue that ESG can improve returns and companies with strong ESG credentials outperform their rivals. It signposts that a company has strong operational and governance controls and is integral to value creation and should be to investment decisions.

Thus far activists are doing a good PR job of choosing ESG campaigns which resonate with the public.

Jana's and the California State Teachers' Retirement Systems' (CalSTRS) targeting of Apple caught the media's eye. Asking Apple to tackle concerns about the harmful effects of smartphone addiction among children and teenagers is certainly important, but Apple is not a company with a poor grasp of ESG; indeed, Jana itself acknowledges that Apple has a history of being responsive to ESG issues.

There have not yet been significant ESG campaigns in Europe. One reason may be that there are still plenty of traditional activist targets, particularly in Germany with its large conglomerates. But another reason might be that European boards take ESG more seriously. A collision between the traditional shareholder model and the broader stakeholder model is now playing out – and rising employee expectations of how their company behaves may support an activist ESG campaign on the continent.

Companies should recognize that activist strategies are constantly changing. Elliott's evolution into part-activist, part-private equity proves this. Activists will shift their focus from a purely value-driven approach to value and ESG as is necessary to succeed. A company with poor governance but a soaring valuation will probably be safe, that is, until the share price falls to the earth.

## SO, ARE YOU READY TO BE YOUR OWN ACTIVIST?

Regardless of which side of this argument you fall, one truism of an attack is that activists can't win on their own; they need to build a consensus to effect change and unlock value. Shareholders – be they traditional asset managers, index funds, retail investors or employees – can have varying and evolving motivations and an activist's platform needs to appeal to all of them.

Geographical nuances also matter. Take Germany, where the approaches between company and activist are usually less aggressive. Activists are increasingly savvy to German business norms and are careful to win over key stakeholders early on, including politicians and employee representatives, as well as shareholders. Elliott is succeeding in Europe by refraining from “shouty” activism. Its first foray into France, targeting Pernod Ricard, has been marked by constructive dialogue (at least for now) and it is using an adviser with local knowledge and connections in Alain Minc, who is close to Emmanuel Macron. Corporate governance changes in Asia, especially Japan, coupled with generational change, have also created an environment in which companies are more willing to engage if activists are seen to be a “force for good.” Activists' approaches reflect this.

All companies must be their own activist. This means proactively addressing vulnerabilities by looking in the mirror, asking are we effectively communicating our strategy and value creation story? Is the right strategy in place for long-term growth? Is this transaction defensible in terms of its rationale and valuation? Are there gaps in our ESG story? It means developing defense narratives and materials, rehearsing responses in simulations and dialing-up stakeholder outreach. It means being transparent about the board's decision making – explaining why the company is not taking certain actions can help rebut activist attack points.

No company, no matter what continent, can afford to be complacent. 📌



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# GOOD GOVERNANCE

WHILE 2018 LACKED A CONCERTED CAMPAIGN ALONG THE LINES OF THE PROXY ACCESS MOVEMENT, SHAREHOLDER RIGHTS ARE BACK IN FOCUS.

An issue that averages 41% support across nearly 70 shareholder proposals and garners majorities at seven of them is clearly something to be reckoned with. Yet support for amending shareholder meeting thresholds, including to as low as 10% of the outstanding shares, received relatively little attention in 2018.

**“NETFLIX HAS LONG BEEN A HOLDOUT AGAINST GIVING INVESTORS MORE POWER.”**

John Chevedden, a frequent shareholder proponent who was behind several of the 2018 proposals, told *Activist Insight* for this report that he chose the issue because it had historically enjoyed good shareholder support. Indeed, BlackRock’s voting policies suggest a company should have a threshold “no higher than 25%,” although it generally favors a 15% minimum. Vanguard, more vaguely, “will generally vote for proposals to grant these rights to shareholders and against proposals to abridge them.”

That does not mean all companies are willing to bend to shareholder pressure. While Cognizant accepted the result of its annual meeting and adopted a 10% threshold, Netflix has long been a holdout against giving investors more power. That it adopted proxy access with far less fuss speaks volumes about how that mechanism was viewed.

Nonetheless, 2018 looked like a good year for shareholder rights on multiple fronts. According to *Activist Insight Governance*, a new database of bylaws and directors, 19 Russell 3000 companies adopted special meeting provisions and 28 amended existing ones in 2018. 39 boards started the process of removing multiyear classes of directors, including former activist targets Fiesta Restaurant Group, Brookdale Senior Living, and Akami Technologies. 17 Russell 3000 companies removed supermajority voting requirements, compared to just 4 adoptions. 2% of the Russell 3000 have active poison pills.

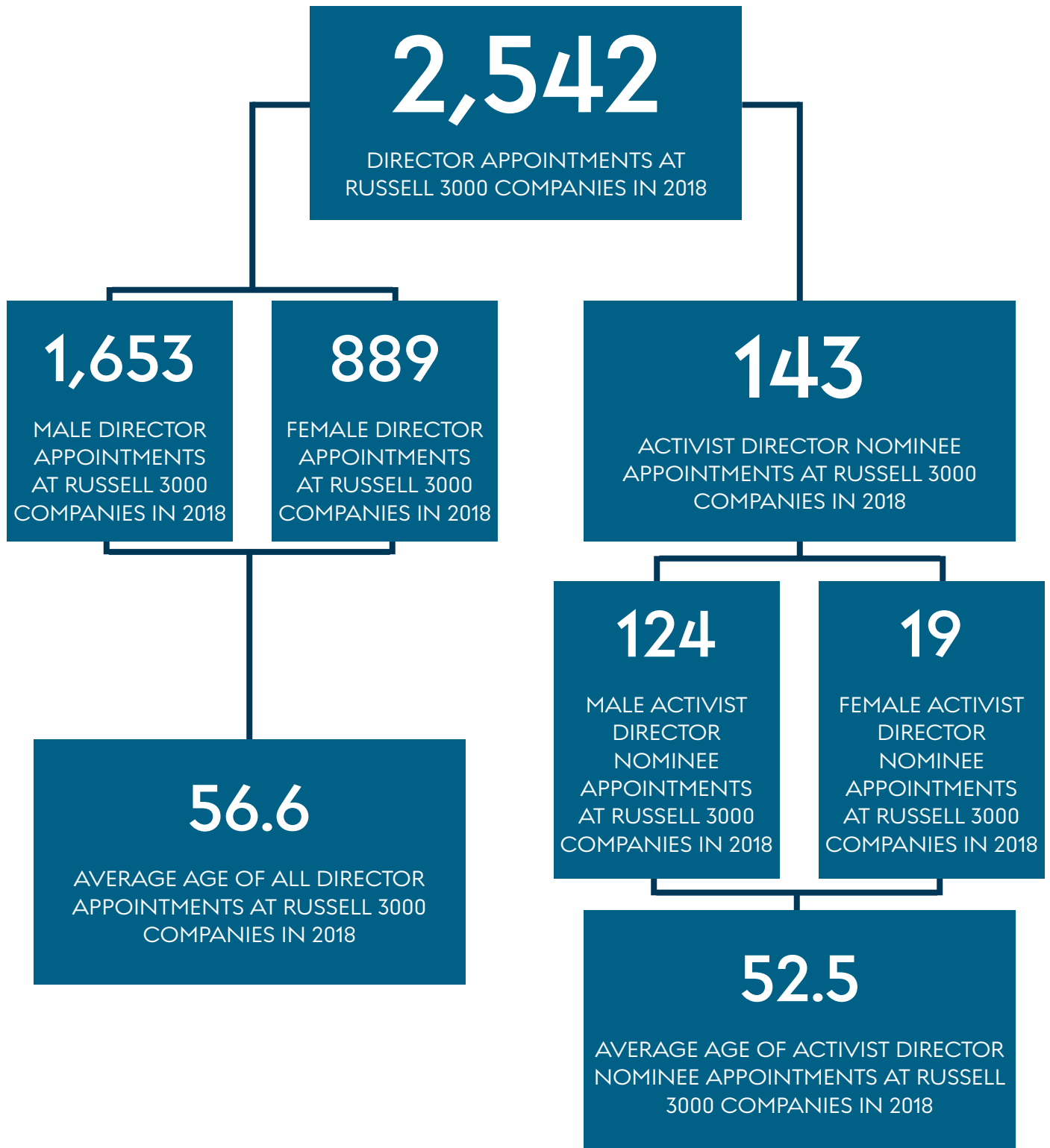
Not that there weren’t reversals in other areas. *Activist Insight Governance* data show that 50% of the S&P 500 Index and 51% of Russell 3000 companies incorporated in Delaware have adopted exclusive forum bylaws, which limit the jurisdictions in which shareholders can bring lawsuits. Shareholder advocates, including those dismissed as “gadflies” can take the good news to heart. In 2018, they focused heavily on governance, according to data from Proxy Insight, which tracks investor voting decisions. For the first time since 2015, shareholder rights proposals outnumbered dissident director elections, with 25% of 2018’s shareholder proposals, versus 15% in 2017.

Perhaps surprisingly, the focus on governance came at the expense of environmental and social (ESG) proposals, topics where mainstream asset managers are starting to show more interest. “Activists are looking for opportunities in the small- and mid-cap space where governance practices may lag market standards,” Anne Sheehan, a senior adviser at PJT Partners told *Activist Insight*. “But you may not always see ESG issues on the proxy because they are frequently being negotiated out.”

**“YOU MAY NOT ALWAYS SEE ESG ISSUES ON THE PROXY BECAUSE THEY ARE FREQUENTLY BEING NEGOTIATED OUT.”**

Whether the change in direction is a reaction – conscious or not – to mooted attempts to push back on shareholder proposals is unclear. Although talk of amending the thresholds for shareholder proposals from the current \$2,000 has surfaced in Congress and at Securities and Exchange Commission (SEC) roundtables, there is little agreement on a path forward. There was no record-breaking year for shareholder proposals as there was for activist investor campaigns, but progress is progress. 🙌

“FOR THE FIRST TIME SINCE 2015, SHAREHOLDER RIGHTS PROPOSALS OUTNUMBERED DISSIDENT DIRECTOR ELECTIONS.”



SOURCE: ACTIVIST INSIGHT GOVERNANCE



# MANAGING THROUGH DISRUPTION

AN INTERVIEW WITH MALCOLM MCKENZIE,  
MANAGING DIRECTOR AT ALVAREZ & MARSAL.



## WHY IS EUROPE CURRENTLY SO APPEALING TO ACTIVISTS?

Ultimately, activist funds' continued success in making good money on their European investments. Crucially, that success is based on the funds learning to adapt their approach to the practice and culture of the country where their target is based. The more positively the funds are viewed by major institutional investors, the more accepted, and therefore successful, they will be. It is a virtuous circle, and one that the funds have learned to adopt.

The above approach can be seen in the recent examples of Nestlé, ThyssenKrupp and Pernod Ricard. This latter approach, by Elliott of course, is particularly noteworthy. Its ultimate success or failure in being accepted as a positive force for good, given the stature and iconic status of the company in French corporate culture, is a bellwether test. If successful, the door to European activism will open even wider.

All of this doesn't mean that Europe will be equal to the U.S. market any time soon, but it is certainly increasingly attractive to activist funds. Our in-house predictive model (A&M Activist Alert - "AAA") is updated every quarter and analyzes all recent trends and activity every quarter. Based on the results of the latest AAA analysis and the predicted targets for future activism, we believe this is set to continue.

## DOES BREXIT GIVE U.K. BUSINESSES A REPRIEVE?

I think we'll see activist activity in the U.K. continue at existing levels or even increase. How different corporates respond to this disruption (ideally proactively and robustly) will vary – some will respond well and others less so. This difference will be demonstrated in their performance and will therefore highlight

**"WE ADOPT A 'NO-HOLDS BARRED' APPROACH BECAUSE, BEING CANDID, THAT IS WHAT THE ACTIVIST FUNDS WILL DO."**

those corporates that have not been as proactive or robust as they should have been. These developments will be closely watched by activists.

## WHERE IS THE MOST ACTIVITY EXPECTED?

Our AAA predictive model predicts that the U.K. will continue to be the most attractive European market for activist funds. Indeed, about 38% of the companies it identified as facing significant risk of activism are U.K. based. France, Germany and the Benelux countries are each at about one third of that level. By sector, industrials are likely to see the most action, followed by consumer and retail (avoiding those corporates that have fallen into the distressed category), and telecoms/technology.

One element worth mentioning is how activists are increasingly targeting companies whose share price is seen as being handicapped with a "conglomerate discount." Where underperforming divisions are driving down the returns on investment, activists are increasingly pressing for either a rapid turnaround of the divisions in question, or simply a divestment.

## HOW SHOULD BOARDS ADDRESS THEIR VULNERABILITIES?

Honest, bi-partisan assessment is essential. We work with boards to undertake a thorough outside-in assessment of how an activist would view their performance, strategy and tactics. We adopt a "no-holds barred" approach because, being candid, that is what the activist funds will do.

Also, the best defense against a potential activist campaign is planned and enacted, not in the battle, but when perceived underperformance starts. It is worth noting that our analysis shows activist funds will now wait less than two years from when underperformance first appears before launching a public campaign. Proactive boards, typically with our candid support, will hunt out areas of underperformance within their business and drive a program to ensure that, before the two years are up, they are at the front of the pack in generating and demonstrating maximum shareholder value. When all is said and done, such great performance is the only true and reliable way of avoiding an activist attack. 🏆



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ALVAREZ & MARSAL



# HOPE-A-DOPE

2018 BROUGHT A ROLLERCOASTER OF DRAMATIC AND UNEXPECTED SITUATIONS ON THE SHORT SIDE, INCLUDING ACTIVISTS PULLING APART THE CANNABIS SECTOR, AND A SINGLE TWEET THAT SENT TESLA ROCKETING AND THEN SPIRALING.

Although activist shorts continued to enjoy a high profile in 2018, the number of campaigns dropped dramatically again in 2018, despite the S&P 500 Index ending the year down 4%. 155 campaigns were launched in 2018, an 18% decrease from 2017 and a 42% decrease from 2016.

As usual the U.S. brought in the most activist short campaigns, with 98 bets against companies. After a recovery in 2017, activist short selling activity rose again in Canada, to 22. In third place, China saw 12 campaigns. A notable change in 2018 was the size of targets: 41% of companies targeted by activist short campaigns had a market capitalization over \$2 billion, up from 29% during 2017.

## TOP TO BOTTOM CYCLES

Unlike in 2017, a year of fraud allegations, the most common allegation in 2018 was misleading accounting. Yet other activist short bets on burgeoning new industries showed renewed hopes that a bear market was in the offing and would burst new bubbles in the cannabis and cryptocurrency sectors.

Activist shorts against cryptocurrencies were starting to kick off at the beginning of 2018. Citron Research ended 2017 covering two of its positions in the sector, citing “easy money” made. Bitcoin Investment Trust, a cryptocurrency firm that Citron said in August 2017 was significantly overvalued as a result of a lack of regulation dropped 16.8% on December 20, 2017. The activist also shorted Riot Blockchain at the end of December 2017 when shares soared nearly 375% after it changed its name in October to reflect its new focus on buying cryptocurrency and blockchain businesses. The shares dropped 11.4% on December 20, 2017.

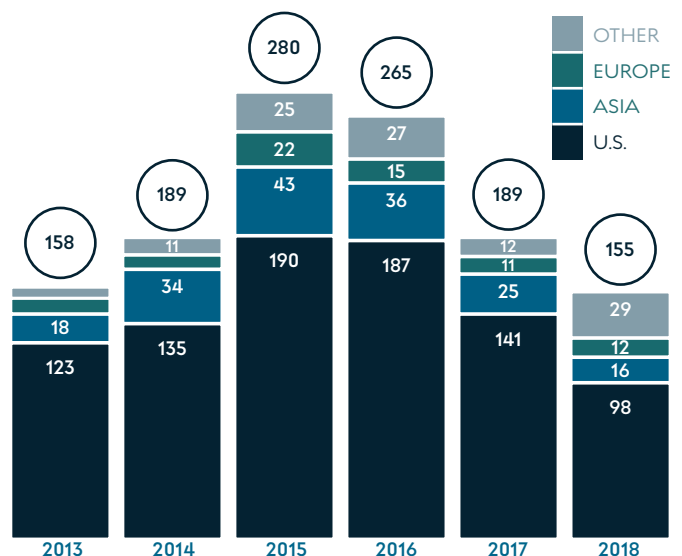
Activist short sellers Xuhua Zhou and The Street Sweeper also gained from bets against Overstock.com’s cryptocurrency venture. The situation gained notoriety with nominal activist short seller Marc Cohodes’ endorsement of management but shares plummeted in March 2018 after it was announced a Securities and Exchange Commission (SEC) investigation would delay the release of its initial coin offering (ICO).

## SMOKED

Another target in 2018 was Tilray, a cannabis researcher and distributor in the healthcare industry that was shorted by Aristides Capital and Citron. Citron switched its position in Tilray from long to short in September after the stock price increased from \$17 per share to \$62 per share in six weeks. Tilray shares shot up 178% within two weeks of Citron revealing its short position but the activist short seller’s founder, Andrew Left, remained adamant and by the end of the year, they had fallen 8.4% since the short seller had gone public. Left told Activist Insight that Tilray is still overvalued. “They’ve priced themselves out of getting any equity deal with anyone,” he says.

Moreover, Left has said there were at least seven cannabis companies cheaper and better positioned than Tilray. He subsequently argued Aphria – a company accused of large-scale fraud by Quintessential Capital Management and Hindenburg Investment Research in December – was a long. Faced with the threat of a hostile buyout and governance changes, Quintessential quit its Aphria bet early in January,

## ACTIVIST SHORT CAMPAIGNS BY YEAR



NUMBER OF ACTIVIST SHORT SELLING CAMPAIGNS BY COMPANY HQ AND BY YEAR (CIRCLED).  
SOURCE: ACTIVIST INSIGHT SHORTS



“COMPETITION AND THE THREAT OF REGULATION IN THE CANNABIS SECTOR MEANS MANY SHORT SELLERS REMAIN EMPHATIC IN THEIR BELIEF THAT THIS COMING YEAR COULD BE DECISIVE.”

despite standing by a thesis that cut the stock almost in half in the days after it was pitched.

## AUTOPILOT CRASH

Arguably one of the biggest moments of 2018 was when Tesla Chairman and CEO Elon Musk posted on Twitter that he might take the company private at \$420 per share, (the share price at the time being \$369.44). The tweet caused weeks of volatility, burning short sellers, until Musk announced that Tesla would remain public, as shareholders opposed the go-private plan. The SEC subsequently settled charges against Musk, with the CEO agreeing to leave his role as chairman and share a \$40 million penalty with Tesla, which was distributed to harmed investors. Citron's Left also sued Musk, alleging that he violated federal securities laws and manipulated the market.

Famed short seller Jim Chanos, founder of Kynikos Associates, said in July that he believed Musk will step down as chief executive by 2020 to focus on other projects. David Einhorn's Greenlight Capital continues to believe Tesla is

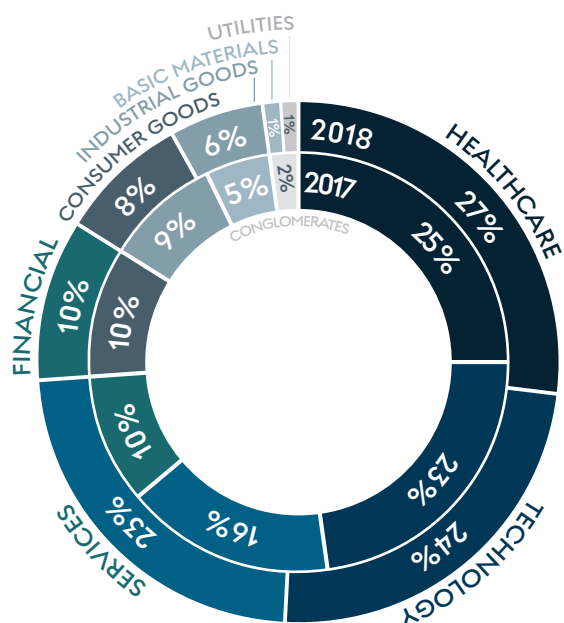
overvalued, while Crispin Odey of Odey Asset Management wrote in a letter to investors that Tesla “feels like it is entering the final stage of its life.”

Despite the mania of last summer, Left made a U-turn with his position in Tesla and went long the stock in October. Left told Activist Insight for this report that “the Tesla story changed because they’ve shown they can make a lot of cars and people want them and they can make profit. I was a skeptic for years saying there’s lots of competition but we haven’t seen any.” Chanos said in an emailed statement, however, “I remain a potential purchaser of [Tesla] shares,” confirming his ongoing short position.

## OUTLOOK

Competition and the threat of regulation in the cannabis sector mean many short sellers remain emphatic in their belief that this coming year could be decisive, as 2018 was in many ways for cryptocurrency stocks. Whether that is the case for Tesla, or for bubbles elsewhere, remains to be seen. 📉

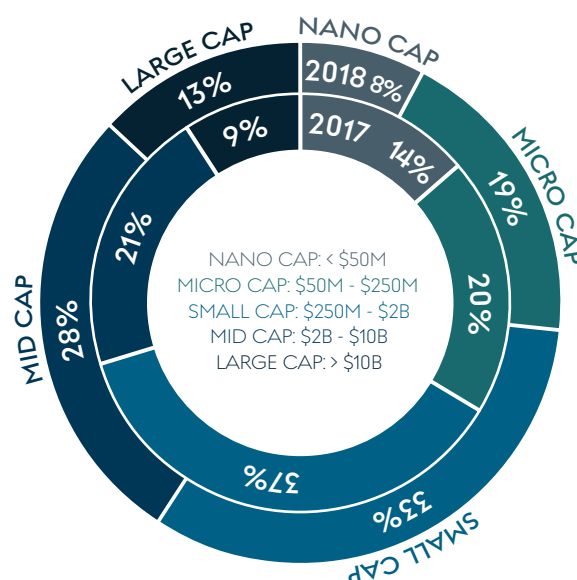
## ACTIVIST SHORT TARGETS BY SECTOR



SECTOR BREAKDOWN OF THE COMPANIES PUBLICLY SUBJECTED TO ACTIVIST SHORT CAMPAIGNS GLOBALLY, IN 2018 AND 2017.

SOURCE: ACTIVIST INSIGHT SHORTS

## ACTIVIST SHORT TARGETS BY MARKET CAP



MARKET CAP BREAKDOWN OF THE COMPANIES PUBLICLY SUBJECTED TO ACTIVIST SHORT CAMPAIGNS GLOBALLY, IN 2018 AND 2017. NOTE: ROUNDING MAY LEAD TO SUMMATION ERRORS. SOURCE: ACTIVIST INSIGHT SHORTS

# THE ACTIVIST SHORT SELLER TOP 5

CITRON RESEARCH RETURNS TO THE TOP SPOT, WHILE SPRUCE POINT CAPITAL MANAGEMENT AND HINDENBURG INVESTMENT RESEARCH REJOIN THE TOP FIVE.

Each year, Activist Insight produces a list of the most impactful activist short sellers of the past 12 months, comprehensively derived from the *Activist Insight Shorts* database. Activist short sellers are ranked by number of campaigns initiated, average one week and one month total campaign returns\*, average size of targeted companies, depth and severity of allegations, company response rate, and news stories written about the activist on *Activist Insight Shorts* in 2018. What follows are Activist Insight's top five activist short sellers of 2018.

\*Total campaign return is a calculation of the stock price change percentage, minus any dividend payment obligations, of campaigns initiated in 2018 from the close prior to the campaign's announcement until the last close on the defined period.

## 01. CITRON RESEARCH

NUMBER OF ACTIVIST SHORT CAMPAIGNS	14
AVERAGE TARGET MARKET CAP	\$25.7B
AVERAGE ONE MONTH TOTAL CAMPAIGN RETURN	3.7%

Veteran short seller Andrew Left experienced a year of ups and downs in 2018 as his Los Angeles-based short selling entity Citron Research placed bets that sometimes fell short of their targets. Citron launched 14 activist short campaigns in 2018, six of which were at companies in the cannabis industry, the hottest new market for attacks of fraud and stock bubbles. Other popular sectors for Citron included technology: with bets against Netflix and Twitter, and biotech, with positions in PolarityTE and Inogen, among others.

Interestingly, the short seller reversed bets against a handful of companies, including Roku, Tesla, and Facebook, contending the stocks will rise. "As a short seller, the most difficult thing to do is acknowledge when the stories change," Left told Activist Insight for this report. "But the best short move I ever did this year [2018] was go long a stock I previously shorted," he continued, referring to Tesla. Left also announced in October that he is raising money to open his first-ever hedge fund, Citron Capital, where he will build short and long investments. The short seller revisited old shorts like Wayfair and Exact Sciences in 2018, but not all the investments were successful. Shares in Wayfair ended 2018 \$60 above Left's \$30 prediction. "I did not like 2018. I thought it was difficult to really hang in there," he said. "I think 2019 is going to be a much better year."

## 02. SPRUCE POINT CAPITAL MGMT.

NUMBER OF ACTIVIST SHORT CAMPAIGNS	14
AVERAGE TARGET MARKET CAP	\$4.2B
AVERAGE ONE MONTH TOTAL CAMPAIGN RETURN	6.0%

With new bets against 14 companies and 15 campaigns continued from previous years, Spruce Point Capital Management had a busy 2018. According to *Activist Insight Shorts* data, the activist focused mainly on small- and mid-cap companies in the technology and services sectors in the U.S. with its usual attention to what it considers misleading accounting. According to Chief Investment Officer Ben Axler, Spruce Point "favored shorting capital dependent businesses with low/no growth, aggressive accounting, and poor governance [last year]. In 2018, the market became much more discriminating between good and bad stock investments. We experienced a healthy and necessary correction."

One of the short seller's most notable campaigns of 2018 was its negative position in Maxar Technologies, a company that Spruce Point labelled worthless in August and said had an unsustainable dividend. The company denied the activist's accusations, but CEO Howard Lance resigned on January 8 and by January 14, the stock had lost nearly 90% of its value since the report had been published. "Much of our concerns about frothy valuations and subdued equity market investment return expectations remain unchanged," Axler explained to Activist Insight. "You can expect more of the same high-quality forensic research and unique ideas from Spruce Point in 2019."

## 03. VICEROY RESEARCH

NUMBER OF ACTIVIST SHORT CAMPAIGNS	7
AVERAGE TARGET MARKET CAP	\$6.4B
AVERAGE ONE MONTH TOTAL CAMPAIGN RETURN	7.2%

Viceroy Research had a year to celebrate in 2018, with three of its 2017 campaigns coming to fruition and playing out “almost word-for-word,” Viceroy Researcher Gabriel Bernarde wrote in an emailed statement to Activist Insight.

Viceroy placed bets against seven companies in 2018, mostly small- and mid-cap, with four of those companies proving the activist right. According to *Activist Insight Shorts* data, the short seller made a 72.2% return on its bet against MiMedx after the stock fell from \$12.34 on September 20, 2017 to \$2.95 on November 8, 2018 when Viceroy exited its position.

Bernarde reiterated his faith in the short seller’s “high-conviction” 2018 reports and sees themes building in the other three targeted companies that would make the campaigns successful. Viceroy is also planning to step into 2019 with “fewer reports on larger enterprises” that are “more concise and accessible to the average person, and [provide] greater engagement with our followers.”

## 04. HINDENBURG RESEARCH

NUMBER OF ACTIVIST SHORT CAMPAIGNS	10
AVERAGE TARGET MARKET CAP	\$868M
AVERAGE ONE MONTH TOTAL CAMPAIGN RETURN	13.7%

In Hindenburg Research’s first full year as a short seller since its 2017 debut, founder Nathan Anderson told Activist Insight that the short seller’s main focus is on corporate fraud. “The desire to unearth these dark secrets is what drives us to dig deep,” he wrote. Hindenburg kicked off 2018 by joining Citron in its short position in cryptocurrency firm Riot Blockchain and after observing several “wacky stories” along the way, finished the year with a joint report on cannabis company Aphria with Quintessential Capital Management. Yangtze River Port & Logistics gave Hindenburg its highest return, according to Activist Insight Shorts, after the short seller claimed the company had fabricated at least 77% of its reported assets and its constructions sites show no signs of business activity.

Hindenburg is showing no signs of slowing down, with Anderson saying that the firm has “some major reports in the pipeline for 2019. I expect some of the guys at these target companies will end up sharing a cell block together,” he adds.

## 05. THE STREET SWEEPER

NUMBER OF ACTIVIST SHORT CAMPAIGNS	10
AVERAGE TARGET MARKET CAP	\$309M
AVERAGE ONE MONTH TOTAL CAMPAIGN RETURN	14.7%

The Street Sweeper continued reporting on stock promotion schemes in nano- and micro-cap companies in the healthcare and technology sectors. Yet it also branched out into the services and consumer goods sectors in 2018, outlining areas where it perceived excessive competitive pressures, medical ineffectiveness, and bubbles it predicted would burst.

While The Street Sweeper’s impact was sometimes mixed, a big compliment was paid by other short sellers following in its wake. Hindenburg jumped on Street Sweeper target Genprex, in May, less than a week after the latter placed its bet, calling it “a long-term zero” but a “dangerous short.” White Diamond also followed The Street Sweeper into Generation Next Franchise Brands’ stock, where it first bet the price would fall to \$1 before reducing it to \$0.30. In a report published by White Diamond, the research firm labelled its short position in Generation Next a “slam dunk,” accusing the company of burning cash and being unsustainable.



# ADVICE BEST TAKEN?

INVESTORS WERE LESS LIKELY TO FOLLOW PROXY ADVISER RECOMMENDATIONS AT U.S. PROXY CONTESTS IN 2018, TAKING A TOUGHER LINE ON DISSIDENTS AND THROWING SKEPTICISM ABOUT THEIR METHODS INTO A HARsher LIGHT, ACCORDING TO DATA FROM PROXY INSIGHT.

Right now, all eyes are on proxy voting advisers. In November, the Securities and Exchange Commission (SEC) held a roundtable on the proxy process, which discussed their alleged conflicts of interest and accusations that firms such as Glass Lewis and Institutional Shareholder Services (ISS) wield too much influence. In December, to rather less fanfare, the Senate Banking Committee held its own hearing on proxy advisers, amid congressional attempts to add layers of regulation to their operations. At the latter event, SEC chair Jay Clayton said new rules could be implemented in 2019.

Against this backdrop, it seems timely to ask how investor voting stacks up against recommendations on proxy contests. If anything, Proxy Insight data suggest the influence of advisers actually seems to be waning.

## ADVISER ALIGNMENT

Looking at the proxy contests that had people talking in 2018, investors simply did not align that closely with either ISS or Glass Lewis. Take Broadcom's attempt to replace the board of rival Qualcomm in order to pave the way for a takeover. This contest was postponed and then ultimately blocked due to national security concerns, but by that point ISS and Glass Lewis had already issued recommendations

and a number of investors had disclosed their voting intentions. Both proxy advisers were recommending a vote on the dissident card, but the majority of the votes we picked up before the postponement supported management's candidates.

Another of 2018's star proxy contests was at Destination Maternity. Shareholders voted to replace the entire four-person board with Nathan Miller's majority-female slate – an outcome at odds with the recommendations of proxy advisers. Both ISS and Glass Lewis had advised their clients to vote the management card, and, what's more, supported all incumbent candidates.

Investors seemed better-aligned with advisers at SandRidge Energy, a meeting notable for using a universal proxy card. ISS and Glass Lewis each supported three of the seven dissident candidates. Two directors had the backing of both advisers, but they disagreed on who the third should be.

Ultimately, five of Carl Icahn's dissidents found their way onto the board. Four of these were elected decisively, and a fifth seat was too close to call, so the company expanded the board to make room without unseating an incumbent. Of the five largest investors tracked by Proxy Insight, BNY

## INVESTOR ALIGNMENT WITH ISS AND GLASS LEWIS

	INVESTOR ALIGNMENT WITH ISS				INVESTOR ALIGNMENT WITH GLASS LEWIS			
	2015	2016	2017	2018	2015	2016	2017	2018
BLACKROCK	42%	73%	60%	36%	42%	73%	75%	36%
SSGA FUNDS MANAGEMENT	50%	67%	67%	46%	50%	67%	73%	46%
BNY MELLON	67%	63%	85%	75%	53%	63%	77%	50%
VANGUARD GROUP	53%	73%	74%	54%	42%	73%	68%	54%
FIDELITY MANAGEMENT & RESEARCH	75%	71%	70%	50%	88%	71%	60%	50%
ALL INVESTOR VOTES	72%	76%	78%	52%	67%	84%	73%	53%

SOURCE: PROXY INSIGHT

“IF ANYTHING, PROXY INSIGHT DATA SUGGEST THE INFLUENCE OF ADVISERS ACTUALLY SEEMS TO BE WANING.”

Mellon showed the strongest alignment with proxy advisers. The firm voted the same card as ISS recommended in 75% of U.S. proxy contests, and with Glass Lewis half the time. The weakest alignment was shown by BlackRock, which matched each proxy adviser 36% of the time.

Interestingly, all five investors aligned much more closely with both advisers in 2017. BlackRock, for instance, matched ISS 60% and Glass Lewis 75% of the time. In fact, in 2018, three of the five investors had a lower level of alignment with each proxy adviser than in any of the previous three years. For context, votes were less aligned with ISS and Glass Lewis during 2018 across all of Proxy Insight’s database. Though results vary by year, the largest investors tend to be less aligned with the proxy advisers than the aggregate.

#### SUPPORT FOR DISSIDENTS

We looked at 18 U.S. proxy contests in 2018, including some that were called off after proxy advisers made their recommendations. We found that Glass Lewis partially or fully supported the dissident card at eight (44%). Proxy Insight was able to collect ISS recommendations for 16 of these meetings, and it supported dissident candidates at nine (56%).

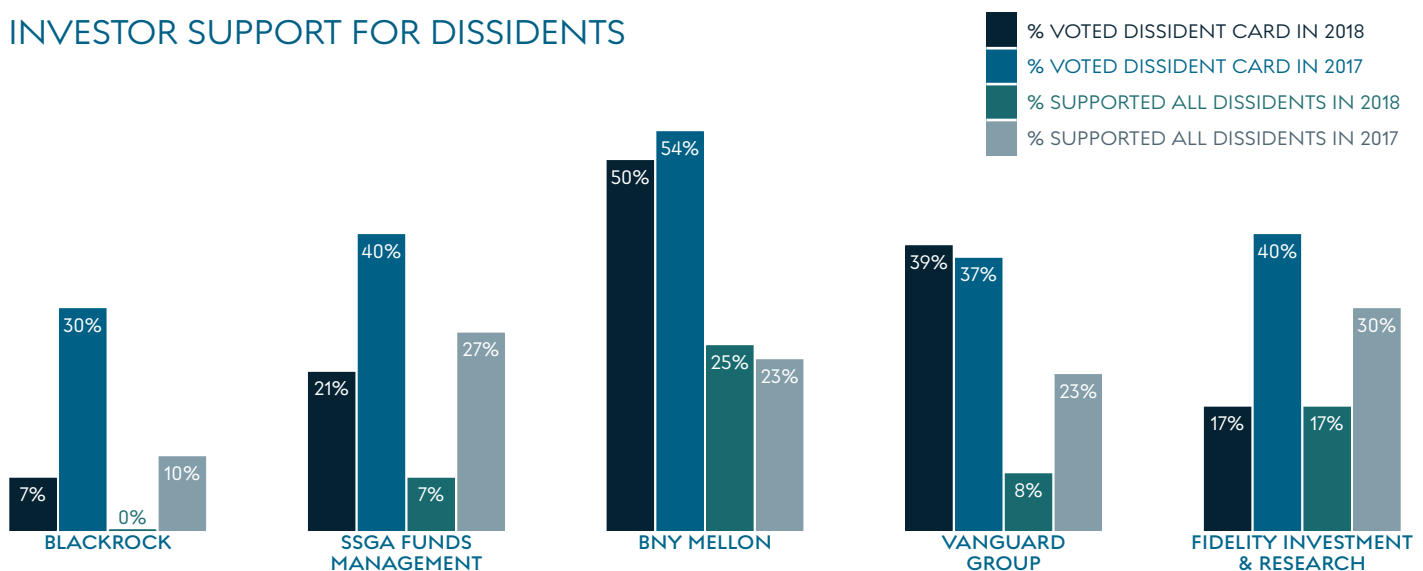
There was plenty of variance in the way top investors voted at proxy contests in 2018. BlackRock, for instance, only supported dissident candidates at one of 14 U.S. proxy contests, SandRidge Energy, and this was only partial support. BNY Mellon, on the other hand, voted the dissident card at half of the eight U.S. proxy contests where it voted, and supported the full dissident slate at a quarter of all contests.

Indeed, of the five largest investors, all except Vanguard voted the dissident card less often in 2018 than in 2017. All except BNY Mellon were less likely to support the full dissident slate in 2018 than the year before. Four of the five also voted on the dissident card less often than either Glass Lewis or ISS recommended.

Investors were also largely less likely to support the full slate than a proxy adviser. Glass Lewis supported the full dissident slate at two meetings, though this includes Taubman Centers where there was only one dissident nominee. ISS supported the full dissident slate at six, again including Taubman Centers.

Whether the shift in voting behaviors translates into a softer approach to regulation is yet to be seen. 🧐

## INVESTOR SUPPORT FOR DISSIDENTS






SOURCE: PROXY INSIGHT

# THE HIT LIST

A HANDPICKED SELECTION OF COMPANIES THAT COULD BE VULNERABLE TO SHAREHOLDER ACTIVISM IN 2019.




## UNITED NATURAL FOODS

VULNERABILITIES	VALUATION 	PERFORMANCE 	OWNERSHIP 
GOVERNANCE ISSUES	COMBINED CEO/CHAIR		
SECTOR	CONSUMER GOODS	TICKER	UNFI
MARKET CAP*	\$666M	1 YEAR TSR*	-71.6%

\* AS OF JANUARY 31, 2019

Wholesale food operator United Natural Foods already has three activists with toehold positions but looks vulnerable to activists taking more significant stakes. Having seen its share price fall nearly 80% throughout 2018, the \$650 million market cap firm could be deemed cheap. A \$2.9 billion acquisition of grocery chain Supervalu is yet to show any clear positive impact and has increased long-term debt ten-fold. Our vulnerability report suggested a breakup of the business could help manage the mounting debt. While *Activist Insight Governance* shows no poison pill, no staggered board, and no dual share-class structure, board entrenchment could form part of an activist's critique given only two directors have been appointed in the last five years. Half of the 10-person board has served for more than 10 years, so an activist could cite boardroom stagnation. The nomination deadline reopens next summer, but a special meeting could be called by 25% of shareholders.

## COLGATE-PALMOLIVE

VULNERABILITIES	VALUATION 	PROFITABILITY 	DIRECTOR TENURE 
GOVERNANCE ISSUES	DIRECTOR PAST RETIREMENT AGE, COMBINED CEO/CHAIR		
SECTOR	CONSUMER GOODS	TICKER	CL
MARKET CAP*	\$56.0B	1 YEAR TSR*	-9.5%

\* AS OF JANUARY 31, 2019

Even though its *Activist Insight Vulnerability*-selected peer group has not seen favorable total shareholder returns over the last 12 months, Colgate has still underperformed the peer median and needs repair. There are currently 11 activists with toeholds in the large-cap stock, albeit with a collective stake of just 0.1%, and an activist could push for its more than \$800 million in excess cash to be invested in emerging markets, where net sales are down, and the Asia-Pacific and Africa/Eurasian regions. Starboard Value, which once held \$12 million worth of shares, sold up in late 2017. In the same year, a Deutsche Bank report said that there was increasing likelihood of an activist targeting the firm. Since then, there have been no major changes to its fortunes, and its share price tumbled more than 20% across 2018.

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# ITRON

VULNERABILITIES	OWNERSHIP 🚩	DIRECTOR SUPPORT 🚩	GROWTH 🚩
GOVERNANCE ISSUES	STAGGERED BOARD, SUPERMAJORITY VOTE		
SECTOR	TECHNOLOGY	TICKER	ITRI
MARKET CAP*	\$2.2B	1 YEAR TSR*	-22.9%

\* AS OF JANUARY 31, 2019

Itron has been deemed one of the companies most vulnerable to activism by *Activist Insight Vulnerability* for more than six months and little has changed: its share price dropped 32% in 2018, earnings were negative for the first time since 2013, and there was continued stagnation at the board level. A lack of board refreshment might stem from the company's staggered board; there have been no new director appointments in three years. Despite seven activists already having a toehold in the company, there have been no activist demands since 2015. Our vulnerability report cited a spinoff or sale opportunity for its traditional metering solutions legacy business, which is in decline in the smart meter era, and still stands as a viable option for an activist.

# COLFAX

VULNERABILITIES	PERFORMANCE 🚩	DIRECTOR SUPPORT 🚩	GROWTH 🚩
GOVERNANCE ISSUES	LONG-TENURED CHAIR, LOW GENDER DIVERSITY, NO PROXY ACCESS		
SECTOR	INDUSTRIAL GOODS	TICKER	CFX
MARKET CAP*	\$2.9B	1 YEAR TSR*	-38.4%

\* AS OF JANUARY 31, 2019

Since our *Activist Insight Vulnerability* report in early November, the commercial machinery firm's struggles have been compounded as its market cap has fallen by more than 20%. 2018 was a difficult year for Colfax: its share price fell by 48% across the year, while share repurchase initiatives worth \$300million have yet to show any signs of success. Terex, of similar market cap within the industrials sector, had an activist initiate personnel changes and sell parts of the business, and has since recovered. If an activist wishes to do something similar at Colfax in 2019, board nominations must be put forward by mid-February. There is significant insider ownership but nothing that hasn't been overcome at other activist targets.

# ACTIVISION BLIZZARD

VULNERABILITIES	DIRECTOR SUPPORT 🚩	BALANCE SHEET 🚩	GROWTH 🚩
GOVERNANCE ISSUES	LONG-TENURED CHAIR, NO SPECIAL MEETING RIGHTS		
SECTOR	TECHNOLOGY	TICKER	ATVI
MARKET CAP*	\$36.0B	1 YEAR TSR*	-35.1%

\* AS OF JANUARY 31, 2019

2018 was no game for Activision Blizzard and 2019 hasn't started well either. The technology giant's share price fell by a total of 28% in 2018 – and more than 40% in the last six months – while both Activision and Blizzard's chief financial officers left within the first week of January to other firms. Concern that some of its video game lines might be getting tired could lead an activist to focus on the more profitable franchises going forward. If an activist were to nominate its own board members, given only one of the firm's current 10 directors was appointed in the past three years, *Activist Insight Governance* shows “activist-friendly” governance provisions: no staggered board, dual-class share structure, poison pill, or controlling shareholder. Insider ownership is also negligible: the 17-strong directors and executive officers own a combined 1.3% of stock. Should an activist wish to make nominations to the board, the deadline for doing so is March 16. 📅



# OUR TRACK RECORD

OUR TWICE-WEEKLY REPORTS ON ACTIVIST INSIGHT VULNERABILITY HAVE ALREADY PICKED UP A NUMBER OF SITUATIONS THAT DEVELOPED INTO CONFRONTATIONS BETWEEN SHAREHOLDERS AND MANAGEMENT.

COMPANY	PAPA JOHN'S INTERNATIONAL
ACTIVIST	LEGION PARTNERS ASSET MANAGEMENT
AIV THESES	BOARD REFRESHMENT, ASSET SALES
PUBLIC DEMANDS	BUSINESS RESTRUCTURING
GAP*	THREE MONTHS

2018 was an eventful year for the pizza chain – its first after founder John Schnatter stepped down as company CEO (replaced by Steve Ritchie). Schnatter's PR disasters saw the share price tumble 30% throughout 2018, leading him to resign as chairman as well. Legion Partners built a 5.5% stake in October and is pushing for new directors.

COMPANY	DENTSPLY SIRONA
ACTIVIST	VALUEACT CAPITAL PARTNERS
AIV THESES	BOARD REFRESHMENT, ISSUE DIVIDENDS
PUBLIC DEMANDS	NONE
GAP*	TWO MONTHS

ValueAct Capital took a small stake in Dentsply Sirona in the third quarter of 2018. 2017 saw an exodus of some high-profile staff after 2016's underwhelming merger between Dentsply and Sirona, as well as spiraling costs. ValueAct often takes board representation at portfolio companies, setting a precedent for Dentsply Sirona.

COMPANY	MACQUARIE INFRASTRUCTURE CO.
ACTIVIST	MOAB CAPITAL PARTNERS
AIV THESES	ASSET SALES
PUBLIC DEMANDS	BOARD CHANGES
GAP*	TWO WEEKS


Moab launched a withhold campaign at Macquarie in May, opposing all six directors two weeks after *Activist Insight Vulnerability* suggested an activist could push for asset sales and board refreshment. Moab struggled to gain traction and may look to raise the stakes in order to better influence company strategy since the stock fell a staggering 45% in 2018.

COMPANY	ASHLAND GLOBAL HOLDINGS
ACTIVIST	CRUISER CAPITAL ADVISORS
AIV THESES	BOARD REFRESHMENT, ISSUE DIVIDENDS
PUBLIC DEMANDS	PROXY CONTEST
GAP*	SIX WEEKS

Six weeks after our evaluation of Ashland's vulnerability, Cruiser Capital built a 2.3% stake, subsequently launching its first ever proxy contest. Prior to Cruiser's announcement, we noted Ashland's "inadequate performance and weak profitability catalyzed by a competitive market, changes in commodity prices, and environmental issues."

COMPANY	EBAY
ACTIVIST	ELLIOTT MANAGEMENT, STARBOARD VALUE
AIV THESES	BUSINESS SPIN OFF
PUBLIC DEMANDS	SALE OF BUSINESS DIVISION
GAP*	THREE MONTHS

2019 could be a make-or-break year for eBay given two new activist positions. Three months after our vulnerability report citing faltering performance of eBay's 11-year-old acquisition, StubHub, Elliott Management and Starboard Value have built holdings, the former making public demands that marry with our report's prediction. Carl Icahn exited his position in eBay in late 2015, after eBay's spinoff of PayPal, and the share price is up only marginally since then.

Dun & Bradstreet was identified as vulnerable to activism in March 2018 and in August sold itself for \$6.9 billion. At *Yelp*, a hot tip in last year's *Activist Investing Annual Review*, SQN Investors voiced concerns and asked for a strategic review. In March, our vulnerability report on **Pitney Bowes** cited the opportunity for a spinoff of its Document Messaging Technologies unit – which then happened a month later without an activist. Elsewhere, **Rite Aid** received a shareholder proposal to spin off its pharmacy benefits management division, Greenlight Capital took a small stake in **Office Depot**, and New Mountain Vantage Advisers entered **LKQ**. 

\*TIME BETWEEN ACTIVIST INSIGHT VULNERABILITY REPORT AND NEW ACTIVIST STAKE DISCLOSED





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