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Citation: Moeller, S., Vitkova, V., Markey, D. & Novikova, A. (2015). The New Normal: The Resurgence of Activist Investing Since the End of the Financial Crisis. London, UK: Mergers & Acquisitions Research Centre (MARC), Cass Business School, City, University of London.

This is the published version of the paper.

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Cass Business School
CITY UNIVERSITY LONDON

The New Normal: The Resurgence of Activist Investing Since the End of the Financial Crisis

M&A Research Centre – MARC

MARC Working Paper Series - 2015



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MARC is the Mergers and Acquisitions Research Centre at Cass Business School, City University London – the first research centre at a major business school to pursue focussed leading-edge research into the global mergers and acquisitions industry.

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Overview

Since 2010 there has been an incredible inflow of capital to hedge funds that focus specifically on activist investing.

The aggressive and often hostile actions of activist funds have created negative publicity and an increased focus on the shortened holding period of these investors. But are activists a blessing or a curse?

This report, produced by the M&A Research Centre (MARC) at Cass Business School provides an insight into the short- and long-term performance effects of activist campaigns in the United States, Germany, and the United Kingdom since the financial crisis.

This report should not be considered as a guide for activist investors on what tactics to use or a guide for company executives on what they should be prepared for. It rather highlights important patterns in the outcomes of shareholder activism in the United States, Germany, and United Kingdom since the beginning of 2010, when the economies of these countries were emerging from the depths of the financial crisis.

Activism tends to be concentrated largely in the United States, but the expectations for further expansion into Europe make it important to understand its existing environment and what activist methods have had success in the region. As equity markets reach new heights in Europe, there will be new opportunities for activist investors.

Highlights of this report:

- *The findings show that in Germany the reaction to activist actions is generally negative, in contrast to the United States (US) and United Kingdom (UK) where long-term performance does show outperformance in some cases.*
- In the United States, activism related to Mergers & Acquisition is shown to be successful. US activists that take short

positions tend to perform poorly. *In both the UK and Germany the results indicate that returns improve considerably when the full length of investments is taken into account.*

- *Activists hold their investments in each jurisdiction for more than one year, and in the UK and Germany, holding periods typically exceed 1.5 years.* These results call into question the accusations that activists are only looking for short-term gains without consideration of the long-term health of a company.
- Based on the length of the activist investments studied, both current and exited, the data indicates that *fears of short-termism may be overblown.* When compared with average equity holding periods the evidence does not suggest that activists take a shorter view than typical investors.
- *The low activity and relatively poor performance in Germany suggests that it is the least receptive market for activists when compared to the US and UK.*
- The evidence shows that *activists could take a more prominent role in the UK* but there is always the possibility that returns will suffer if more activists pile in.
- The *United States is the undisputed leader of shareholder activism* but despite its commonality, the performance from investors shows that finding the right approach remains challenging.

Is Activist Investment Equivalent to Short Termism?

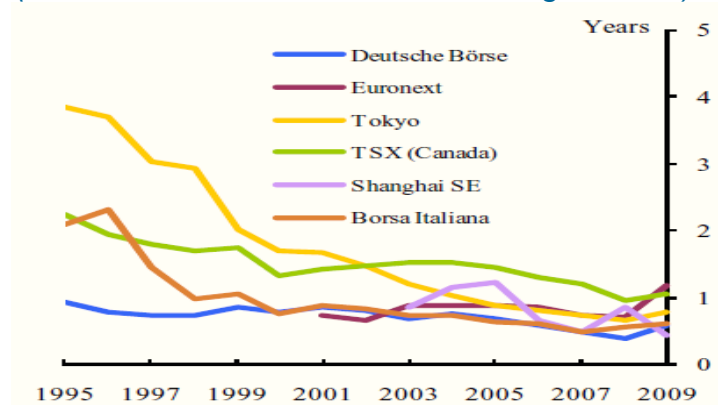
The idea that activism is representative of “short-termism” is one that is up for debate. Data from various sources indicates that declining holding periods for equities is decades in the making and not a recent phenomenon to be blamed on shareholder activism. Despite research touting the benefits of long-term share ownership, the holding period on the NYSE, LSE, and Deutsche Börse has been less than two years for at least the past two decades, as presented in Figure 1 below.

In many cases activists are criticized not regarding the length of engagement, but for their tactics. In particular, many are critical about the use of buybacks or special dividends to reward shareholders. It is argued that this type of outcome fails to consider the ramifications of the lack of capital investment

and the impact this will eventually have on future growth. Special dividends and share buybacks can also result in artificially boosted share prices and stock-based compensation for executive¹.

The solution to the perceived problem is hard to determine. Frequent critic of short-termism Harvard Business Review, puts the challenge to institutional investors to be good corporate stewards and make sure strategy is aligned for the long-term.² However, as pointed out in its 2014 review of activism, some of the largest, most powerful institutional investors are increasingly backing activists in their campaigns for change.³ At the height of the 2007 pre-crisis activism boom evidence showed simply that open dialogue and focus on improving performance led to the best outcomes.⁴

Figure 1 – Average holding period for global equity exchanges (Source: World Federation of Exchanges, 2015)



¹ Lazonick, W., 2012. In the Name of Shareholder Value: How Executive Pay and Stock Buybacks are Damaging the US Economy. In Clarke, T. & Branson, D. The SAGE Handbook of Corporate Governance. London: SAGE Publications Ltd. pp.476-96.

² Barton, D. & Marc, W., 2014. Focusing Capital on the Long Term. *Harvard Business Review*, January-February(1), p.8

³ Activist Insight, 2015. Activist Investing - An annual review of trends in shareholder activism. Research. London: Activist Insight.

⁴ MacGregor, J. & Campbell, I., 2007. Dealing with investor activism: Investors seek cash returns from pushing your buttons - There are things you can do to prepare for an attack. *International Journal of Disclosure and Government*, 5(1), pp.23-35

Investing Landscape Across Different Geographies

Of the myriad challenges investors face in looking for opportunities is the different regulatory environment of each country. While legislative changes over the past two decades have brought more continuity, subtle nuances still exist between most major equity markets. Understanding the investing environment is critical for investors and provides insight into the likelihood and outcome of activist engagements. Comparing the likes of the United States, United Kingdom, and Germany it is possible to contrast how even slight differences in the regulatory frameworks play an important role in determining how activism is approached. The working paper from Becht Franks and Grant provides a useful guide to the current environment, and is used as the baseline for this comparison.⁵ Where relevant, this report examines any updates or proposed changes in the selected countries.

Included among the most important tools in an activist's arsenal are the ability to remove directors, nominate new directors or entire boards, call shareholder meetings, make proposals, and act in concert with other shareholders. Along the way investors must take into account reporting requirements and be vigilant about the disclosures it makes. This is where things begin to diverge for investors looking at opportunities in different geographies. For instance, the United States uses plurality voting in board elections, meaning certain directors can still be elected with less than 50% approval (including abstentions). The UK and Germany use a simple majority. However, when it comes to removing a director before the end of their tenure Germany joins the US in mandating that

a director can only be removed "for cause," and Germany goes one step further by requiring a supermajority vote. Shareholders in the UK need only a simple majority and can remove directors without cause.⁶

Interestingly, despite the prevalence of activism in the US, it is perhaps the most difficult environment for any investors to actually have proposals voted upon. Shareholders have no legal right to call an extraordinary general meeting (EGM), unlike each of the other four. In 2009 the ownership threshold for calling an EGM in the UK rose from 5% to 10%, while in Germany it is 5%. In addition, even if proposals from shareholders make it to a vote in the US, the results are only advisory. In the UK and Germany all shareholder proposals are binding.⁷ This might help explain why shareholder proposals in these countries often do not pass. Where each of these countries shares commonality is in the cost of proxy solicitation, which is carried by the shareholder. This is important, as it is estimated to cost anywhere between \$200,000 and \$1m by advisory firm Georgeson.⁸ Lastly, it is important to note what preventative measures companies can implement, through control-enhancing mechanisms, shareholder rights plans, and mandatory bid rules. In the US investors are more likely to encounter poison pills, the use of which has been declared legal by their respective court systems under legal challenges within the past ten years. Meanwhile, in the UK and Germany investors must take note of mandatory bid rules. Set at

⁵ Becht, M., Franks, J., Grant, J. & Wagner, H., 2014. The Returns to Hedge Fund Activism: An International Study. *European Corporate Governance Institute*. Working Paper.

⁶ Ibid.

⁷ Ibid.

⁸ Kumar, R., 2014. *2014 Annual Corporate Governance Review*. Research. New York: Georgeson. <http://www.georgeson.com/us/resource/Pages/acgr.aspx>.

30% in the UK⁹ and Germany¹⁰ any shareholder exceeding these levels must propose a full acquisition.

Yet little in the world of investing often stays the same for very long. In 2010, with the passage of the Dodd-Frank legislation in the United States, formally known as the Wall Street Reform and Consumer Protection Act, originally included a mandate for universal ballots. This would force companies to include all shareholder proposals on a single ballot, potentially saving millions for activists. However, the legality of this measure was challenged and overturned. After years of voicing their displeasure the tide may be turning back in activists' favour, as the Chairwoman of the SEC Mary Jo White voiced support of universal ballots and it will be voted on by the regulator's five commissioners and with a majority will pass.¹¹ Separately in France in 2014, the government passed what has become known as the Florange Law. The law forces all public companies listed in France to reward long-term shareholders, those owning shares for over two years, with double voting rights.¹² Following France's lead, legislation is currently working its way through European Commission regulatory bodies that would apply to all companies in the EU.¹³ While companies can, and have, changed their by-laws to maintain one-share, one-vote rules, it does give considerable power to large shareholders of public companies, and thus the opposite for activists seeking to build stakes and make changes.

⁹ The Takeover Panel, 2015. *The Takeover Code*. Regulatory. London: RR Donnelly The Takeover Panel.

¹⁰ Korsch, H.S. & Eichwald, D., 2014. *Germany Takeover Guide*. Regulatory. Mutze Korsch Rechtsanwaltsgesellschaft mbH.

¹¹ Ackerman, A. & Benoit, D., 2015. *SEC Chief Tilts Again to Activists*. [Online] Available at: <http://www.wsj.com/articles/sec-chief-calls-for-new-corporate-ballot-rules-1435240995> [Accessed 26 June 2015].

¹² Strothard, M., 2015. *French companies fight back against Florange double-vote law*. [Online] Available

Equity Markets in the United States, Germany, and United Kingdom

It is necessary to evaluate the marketplace within which the shares of targets of activist campaigns are traded. Activism tends to be more prevalent in the equity markets of the New York Stock Exchange (NYSE) and the National Association of Securities Dealers Automated Quotations (NASDAQ), totalling approximately \$27 trillion compared to the Deutsche Börse where activism accounts for slightly more than \$1.8 trillion. Meanwhile, despite the London Stock Exchange including over 2,700 listed entities, more than the NYSE and only slightly less than the NASDAQ, its total market capitalization is approximately \$4.3 trillion, about 56% of the NASDAQ and 22% of the NYSE.¹⁴ Proportionally, the number of companies subject to an activist campaign is also larger in the US (20% of US listed companies are the subject of an activist campaigns), than in the UK (5% of UK listed companies are the subject of an activist campaigns) and Germany (3% of German listed companies are the subject of an activist campaigns).

Figure 2 below highlight the differences between the US, UK, and German equity markets and make clear that investors are operating in a much larger universe in the United States. There have been activist campaigns against more NYSE and NASDAQ-listed companies in the United States (1,060) than there are listed companies on the entire Deutsche Börse (647). Yet it is clear that size is not the only factor at work, for if it were, then proportionally the number of companies subject to an activist campaign would be equal.

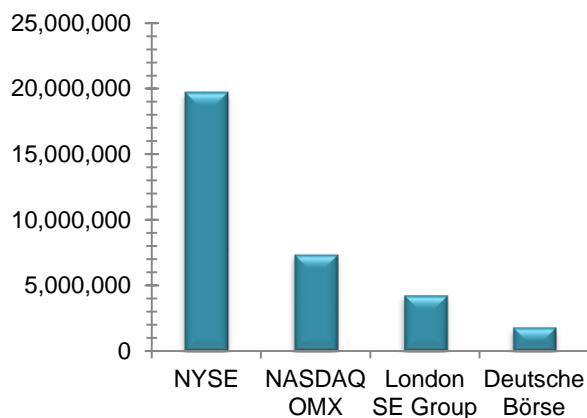
at: <http://www.ft.com/cms/s/0/05314dfe-e27d-11e4-ba33-00144feab7de.html#axzz3jLkPQ1At> [Accessed 28 June 2015].

¹³ EurActiv, 2015. *EU lawmakers back rewards for long-term shareholders*. [Online] Available at: <http://www.euractiv.com/sections/euro-finance/eu-lawmakers-back-rewards-long-term-shareholders-314439> [Accessed 28 June 2015].

¹⁴ World Federation of Exchanges, 2015. *Statistics*. [Online] Available at: <http://www.world-exchanges.org/statistics>

However, approximately 20% of US-listed companies have been subject to an activist campaign since 2010 that figure drops to less than 5% in the UK and less than 3% in Germany.

Figure 2: Market Capitalisation per exchange (Source: World Federation of Exchanges, 2015)



A Closer Look at Germany

The stakeholder model that characterizes Germany's corporate culture has several important distinctions between it and the models favoured in the US and UK. Ownership has long been characterised by large blockholders including banks, insurance companies, industrials, and families, often in a complex web of cross-shareholdings. Two-tier boards include far more stakeholder representation in Germany than its Anglo-American counterparts. Codetermination requirements give employees a say in the management of their companies, while banks have long had a seat on supervisory boards. Even in light of several efforts to invigorate

public equity markets through legislative efforts there is scant evidence to suggest Germany will move towards a more shareholder-focused model in the near future, given that it would like face stiff government and labour union opposition.¹⁵ Thus the deck remains stacked against activists looking towards Germany.

Two notable changes to the German landscape occurred in 1998 and 2000, with the passing of Control and Transparency in Business Act (KonTraG) and reforms to corporate tax law in 2000. Introduction of KonTraG not only helped reduce cross-shareholdings through restrictions on voting rights but also helped give rise to retail investor proxy associations, which typically held long-term interests and had fewer conflicts of interest.¹⁶ Meanwhile, the tax reforms enacted in 2000 abolished corporate income tax for companies liquidating long-term shareholdings, which was shown to have a drastic downward effect on the number and average size of large block shareholdings and cross-shareholdings, particularly in the financial sector.¹⁷ The above mentioned regulatory changes gave more power to minority shareholders and attracted more foreign capital.¹⁸ However, despite ownership concentrations coming down since 2000, the necessary market conditions for challenging corporate control are still far from prevalent in Germany. An analysis of shareholder engagement from 2008 to 2010 indicated that 40% of counter motions to board proposals came from retail proxy associations, while just 2% originated with institutions.¹⁹ Additional studies on activism in Europe supported the hypothesis that high ownership concentration had a negative correlation to shareholder activism.²⁰ In situations when proposals from

¹⁵ Sudarsanam, S. & Broadhurst, T., 2012. Corporate governance convergence in Germany through shareholder activism: Impact of the Deutsche Boerse bid for London Stock Exchange. *Journal of Management and Governance*, 16(2), pp.235-68.

¹⁶ Strätling, R., 2012. How to overcome shareholder apathy in corporate governance - the role of investor associations in Germany. *Annals of Public & Cooperative Economics*, 83(2), pp.143-57.

¹⁷ Weber, A., 2009. An empirical analysis of the 2000 corporate tax reform in Germany: Effects on

ownership and control in listed companies. *International Review of Law & Economics*, 29(1), pp.57-66.

¹⁸ Ibid.

¹⁹ Schaefer, H. & Hertrich, C., 2013. Shareholder Activism in Germany: An Empirical Study. *IUP Journal of Corporate Governance*, 12(2), pp.28-39.

²⁰ Judge, W., Gaur, A. & Muller-Kahle, M., 2010. Antecedents of Shareholder Activism in Target Firms: Evidence from a Multi-Country Study. *Corporate Governance: An International Review*, 18(4), pp.258-73.

activists are voted on at AGMs there is seen to be a negative effect on share prices attributed to the significance these matters indicate in Continental Europe, attributable to proposals legally binding nature and a far cry from their use (or overuse) in the US.²¹

The famous recent example of shareholder activism influencing management strategy from the failed Deutsche Börse-London Stock Exchange merger shows how German firms with dispersed ownership are more at risk.²² However, in general, the evidence is against hedge funds and private equity firms being able to force management changes at German firms, and in the case of hedge funds it's actually the opposite.²³ In fact, implementation of the Risk Limitation Act in 2012 makes it increasingly difficult for activists to implement their plans, adding to previous disclosure requirements. Shareholders exceeding 10% must declare their intentions within 20 days, which follows US and French norms. In addition, the changes widen the scope for what German regulators consider to be shareholders "acting in concert" to push a specific agenda. Not only must coordinated efforts be disclosed, but also closely monitored to determine whether combined holdings breach 30%, which would trigger a mandatory takeover offer. This is a potential explanation for increased activism through litigation following merger announcements, pushing for higher transaction premiums as opposed to waging lengthy campaigns.²⁴

Activist Targets based on Size and Sector

A global breakdown of campaigns since the beginning of 2010 through June 2015 based on

market capitalization is presented in Figure 3. The data is broken down into five categories from Nano-cap as the smallest to large cap at the top of the range. Nano-cap companies are those that were under \$50m in market capitalization at the time of engagement, with micro-cap from \$50-250m, small cap from \$250m to \$2bn, mid-cap from \$2bn to \$10bn and large cap including any target with a market capitalization above \$10bn. The information provides insights into the typical size targets in which activists are taking positions during a given year. Given the expected returns from companies of different sizes – typically small cap companies can produce larger returns on a per cent basis – this is important to evaluate. With the exception of 2011, when micro-cap targets slightly exceeded them, small cap companies have been the most targeted. On a per cent basis, about 25% of engagements each year target small cap companies, while micro-cap is nearer to 20% per year. The most significant changes are at each end of the spectrum, with Nano-caps being targeted far less dropping from almost 20% in 2010 to barely above 10% in 2015.

Figure 4 shows the sector categories that have been targeted since 2010, providing insight into where activists have been focusing their efforts. Companies operating in the Services, Financial, and Technology sectors have been the most heavily targeted each year since 2010 accounting for at least 57% of investments in each year and in total representing over 60% of all investments.

Sauerwald, S., Van Essen, M. & Van Oosterhout, H., 2013. Shareholder Activism in Europe: Evidence from Shareholder Dissent in France, Germany, and the UK. *Journal of Corporate Governance*, pp.552-57.

²¹ Cziraki, P., Renneboog, L. & Szilagyi, P., 2010. Shareholder Activism through Proxy Proposals: The European Perspective. *European Financial Management*, 16(5), pp.738-77.

²² Sudarsanam, S. & Broadhurst, T., 2012. Corporate governance convergence in Germany through shareholder activism: Impact of the

Deutsche Boerse bid for London Stock Exchange. *Journal of Management and Governance*, 16(2), pp.235-68.

²³ Voubem, B., Schäffer, U. & Schweizer, D., 2014. Top management turnover under the influence of activist investors. *Journal of Management and Governance*, 19(3), pp.709-39.

²⁴ Besse, D. & Heuser, M., 2014. Shareholder Activism in Germany Following a Takeover Announcement. *Attorney Advertising*, 27 May. pp.1-3.

Figure 3: Activist Actions by Market Cap since 2010
 (Source: Activist Insight, 2015)²⁵

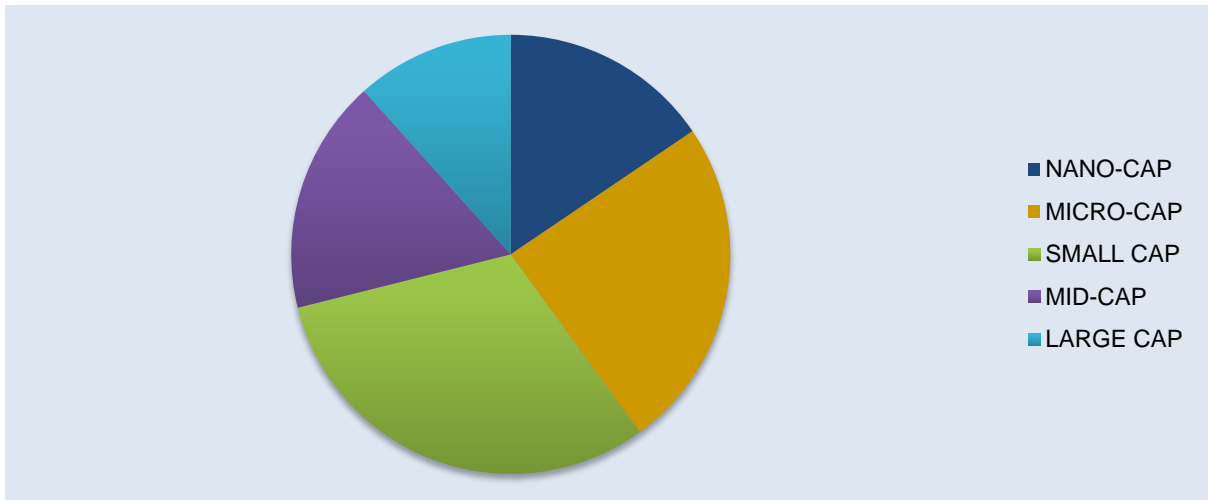
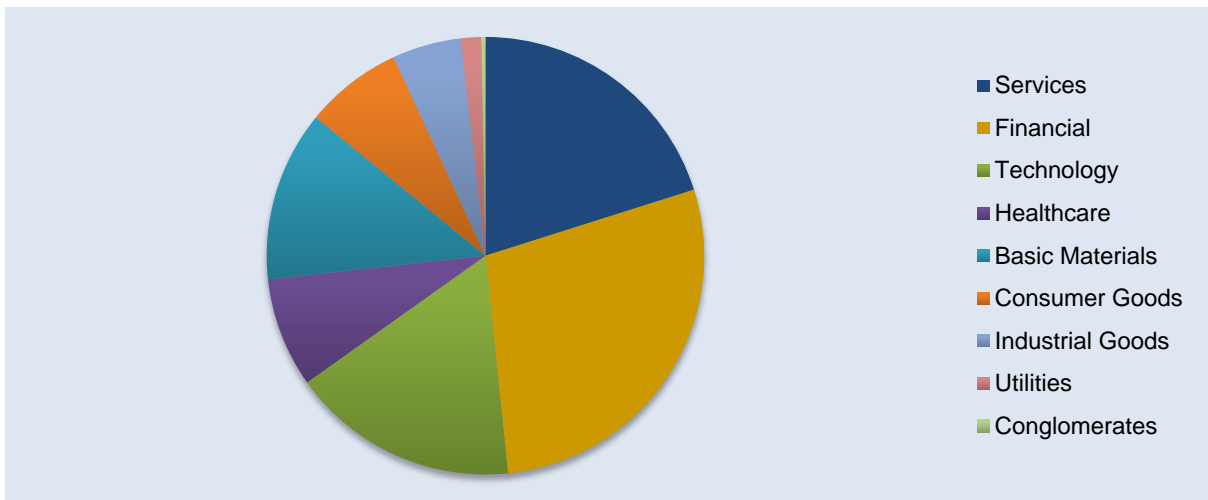


Figure 4: Activist Actions by Sector
 (Source: Activist Insight, 2015)



²⁵ Activist Insight, 2015. *Public Action Report*. [Spreadsheet] London: Activist Insight Available at: www.activistinsight.com.

Performance Implications of Activist Actions

Short-term Reaction in the United States

This section of the report focuses on the analysis of short-term market reaction to the announcements of activist campaigns.²⁶ The data results are broken down to show the ten-day pre-event returns (i.e. before the announcement of a given campaign), event day returns (i.e. on the day of campaign announcement), and ten-day post-event returns (i.e. following the announcement of a given campaign). The “Action Date” is used as the announcement day.²⁷

If the data shows that returns on the event day and in the post-event ten-day trading window are greater than zero it lends support to the argument that the market reacts positively to activist actions. The reverse is true if the abnormal returns are negative.

The mean return for each period is positive, with pre-event returns highest at 2.78%, with mean post-event returns of 0.43% and mean event day returns of 0.005%. The results also show high degrees of volatility. Both the event day and post-event returns display characteristics of normally distributed data around the mean. The pre-event returns show the returns are positively skewed. The results are surprising in that they show stronger pre-event performance than event day or post-event performance. The hypothesis that the announcement of a campaign generates positive abnormal returns is not supported for the full period. These

results are the opposite of what was anticipated at the start of the study.

Tables 1 & 2 summarize the data on a year-by-year basis, showing how market reactions have differed. Pre-event returns are the strongest in the majority of periods, only bested in 2011 when the average impact on target share prices was negative.²⁸ The results on a year-by-year basis are consistent with the overall sample results, with mean pre-event returns showing significant differences in three of five-plus years²⁹, while mean event day returns are different in two years (in one case below the mean index return – 2013). There is no statistically significant evidence to support a presence of abnormal returns following the announcements of activist campaigns in any year.

The year-by-year data also does not support the original hypothesis strongly, but does show that in certain years there was a measurable positive abnormal return for target companies. The results could indicate that investors are hesitant to quickly decide on the merits of an activist investment, knowing that resolution could be a long way off. It is possible that the capital markets are waiting to base their decision on additional information being presented.

²⁶ Share prices for the 21-day event study were retrieved from Bloomberg databases and matched with information from the Activist Insight database.

²⁷ The “Action Date” is used as the event day, as this coincides with the registration of a 13d SEC filing or press release by activist investors. The Action Date is often not the same as the initial investment date. To study event returns that ten days before and after the Action date were included in the sample.

²⁸ To determine whether the difference between the mean of the two data sets t-tests were performed with reliability levels of 5%. In each case the null hypothesis (H_0) is that the difference between the mean target return and the mean index return is zero. The alternative hypothesis (H_a) is that the mean target return is not equal to the mean index return. Only in the case of pre-event returns is there support for rejecting the null hypothesis

²⁹ Statistically significant.

*Table 1: US Event Window Returns
(Source: Bloomberg)*

	Target Pre-Event	Target Event Day	Target Post-Event	Market Pre-Event	Market Event Day	Market Post-Event
2010	1.98%	1.48%	0.98%	0.49%	0.22%	0.69%
2011	-0.48%	-0.29%	-0.99%	0.09%	-0.08%	0.06%
2012	4.25%	0.53%	-0.26%	0.42%	0.05%	0.47%
2013	3.69%	-0.51%	1.05%	0.99%	0.08%	0.70%
2014	0.51%	-0.05%	0.17%	0.42%	0.11%	0.49%
2015	7.34%	-0.71%	1.47%	0.23%	0.03%	0.14%

*Table 2: US Event Window Abnormal Returns
(Source: Bloomberg)*

	Pre-Event AR ³⁰	Event Day AR	Post-Event AR	CAR	CAR Event+ ³¹
2010	2.00%	1.00%	0.00%	3.00%	2.00%
2011	-0.56%	-0.22%	-1.09%	-1.87%	-1.31%
2012	3.77%	0.49%	-0.73%	3.53%	-0.24%
2013	2.68%	-0.59%	0.36%	2.00%	0.00%
2014	0.07%	-0.16%	-0.31%	-0.40%	-0.47%
2015	7.07%	-0.74%	1.34%	7.67%	0.60%

³⁰ "AR" represents abnormal returns, the difference between the average returns on the target and average returns on the S&P 500 index.

³¹ CAR Event+ is a measure of the combined cumulative abnormal returns on the event day and during the post-event ten-day window. It excludes pre-event returns.

Short-term Reaction in the United Kingdom

Activist targets have positive average returns in each of the pre-announcement, announcement day and post-announcement periods. Notably, the UK is the only region in which the average target returns exceed the average index returns in all three periods. In the pre-announcement period the average index-adjusted return over the entire period (i.e. before, during and after campaign announcement) for the activist targets is 2.48%, the highest compared to the US and Germany. The average index-adjusted return for each of the pre-announcement, announcement day, and post- announcement periods is 1.65%, 0.26%, and 0.56% respectively, again the only sample with positive mean CARs in each period.

The results demonstrate that while targets are outperforming in the immediate period prior to the announcement of an action, they lose this momentum once the action is announced. Although the expectation that the announcement of an activist campaign generates abnormal returns is not supported by the analysis, it could indicate other conclusions. It is possible that fund managers are trying to time their actions to align with the positive momentum of the targets' recent performance hoping it will continue.

Short-term Reaction in Germany

In contrast to the US and the UK, the average returns in the ten-day pre-announcement trading period for activist targets in Germany is -0.99% (negative), while the German Stock Index (DAX) average return is 0.52%. On the action date activist targets average a positive return of 0.50%, a number that is marginally above the DAX average return of 0.36%. In the ten-day post-announcement trading period activist targets reverted to negative average returns, in this case -1.36% while the mean return from the DAX during the same trading period is 1.02%. Compared to the short-term market reaction in the United States, the variance in the results in Germany is lower and trading is within much smaller ranges in each of

the three periods, before, on, and after the announcement of an activist campaign. Comparing the average target and index returns following the announcement of activist campaigns shows that target returns were lower than index returns (-2.37%).

Looking at the cumulative abnormal returns surrounding the announcement of an activist campaign for German targets, the results for both the entire announcement period as well as announcement day plus next ten trading days show negative returns. This finding indicates that the immediate perception of activist actions by the German capital markets is negative. The mean abnormal return for the entire 21-day event period is -3.69% and the mean abnormal return for the period including the announcement day and following ten trading days is -2.23%.

The target returns on the date of announcement are not significantly different from zero, implying that the shares pause their negative momentum on the day of the campaign announcement before continuing to fall over the next ten days. This finding indicates that investors do take note of the actions of activists, but these actions do not serve to reverse the negative pre-announcement performance. In this respect Germany differs from both United States and United Kingdom. The analysis demonstrates that shareholder activism is looked upon negatively in Germany, which is also reflected later in the long-term returns.

Long-term Performance in the United States

The analysis of the long-term effects of activist campaigns in the United States looks at investor returns from four perspectives: by market capitalization, activist action, company response, and campaign outcome.

The data shows that target firms had an average return in the month prior to a given announcement of 4.91%. The average buy-

and-hold abnormal return was 3.53%.³² To evaluate the post- announcement returns to targeted firms the one-year period following the announcement of an action was examined, providing an average target return of 15.03%. However, in the matching one year post-action period the market also averaged significant gains of 15.58%, and therefore the buy-and-hold abnormal return to investors in activist targets was actually negative -0.29%.³³ In total, only 313 of the 716 events had positive long-term abnormal returns. The returns were measured a final time to determine whether there is a difference in outcomes between long and short investing (i.e. the position that activists take on the target company).

The results shows that activist investors who took a long position gained a mean abnormal return of 3.49%, while short activists suffered mean losses in year one of -12.90%.³⁴ This finding shows an important distinction between

the success of long and short activists that plays out consistently in the analysis of the United States.

All further long-term analysis was done using the performance of returns through the exit date or current period. Campaign outcomes in the United States are broken down into seven categories – Activist Successful, Activist Partially Successful, Activist Unsuccessful, Compromise/Settlement, Unresolved, Withdrew Demands, and Withdrew Board Nominations. In total 957 campaigns are included in the initial sample. Out of these, 67% (643) are either successful or partially successful. Activists withdrew their demands or board nominations in less than 10% (77) of cases, while unsuccessful and unresolved campaigns make up the remaining 25% (237) of events. The average returns are presented in Table 3.

*Table 3 – US Activist Returns by Campaign Outcome
(Source: Bloomberg)*

Outcome	No. of Investments	Average Follower Return	Average S&P Change	Average BHAR
Activist Successful	455	37.67	11.69	23.61%
Activist Unsuccessful	185	36.65	12.35	12.97%
Compromise/Settlement	99	23.78	11.85	8.55%
Withdrew Demands	38	21.57	13.87	6.44%
Unresolved	52	19.46	14.07	4.40%
Withdrew Board Nominations	39	12.88	9.98	2.67%
Activist Partially Successful	89	12.92	11.49	0.44%

³² The results were found to be statistically greater than zero.

³³ Further testing has shown that results were not significantly different from zero.

³⁴ Both results were found to be statistically greater than or less than zero.

Of these figures, only the Successful campaigns produce long-term returns that are statistically greater than zero. If the results are run a second time, with the exclusion of extreme values from the sample, the returns are far lower and no outcome exhibits statistically significant results. The second set of results makes it clear how much one or two extreme values can affect the outcomes. The returns to Successful and Unsuccessful campaigns drop by more than 20% with just two and one campaigns excluded, respectively. Moreover, it means that the long-term returns for investors are not statistically different from zero. While campaigns categorised as Compromise/Settlement and Withdrew Nominations show clear differences between target and index returns, the follower returns for both are positively skewed (though not as much as the Successful and Unsuccessful campaigns including all events), indicating that even without extreme values the averages can be affected.

If the presented results are broken down further to separate them by industry, the only categories that show long-term returns that are statistically greater than zero are Healthcare (14.44%) and Technology (107.48%/16.43%) in Successful campaigns and Technology in Unresolved campaigns (27.87%). Basic Materials targets are consistent underperformers with negative long-term returns in all outcomes and returns that are statistically less than zero in Successful (-27.29%), Partially Successful (-23.87%), and Compromise/Settlement (-15.93%) situations. The only other statistically significant outcome is Financial Services targets in Partially Successful campaigns with a negative return of 7.36%. Long-term returns calculated by outcome and company size (market capitalization) show that positive returns are more consistent for Small Cap and Mid Cap targets than any other size³⁵.

Measuring returns by the type of activism an investor employs provides a granular look into

the data. The 44 sub-types are condensed into eight main categories – Activist Short, Balance Sheet, Board-related, Business Strategy, M&A, Other Governance, Other, and Remuneration. The three most popular categories of activism are Board-related (490), Activist Short (277), and M&A (272), while Balance Sheet (158) and Business Strategy (121) are less popular types of activism. The only two categories to deliver long-term returns that are different from zero are M&A and Activist Short. M&A Activism provides abnormal returns of 29.45%. Activist Short actions deliver returns of -7.73%, the worst of any category.

The long-term campaign data from the United States taken as a whole does not support the proposition that activists achieve abnormal returns greater than zero, but the analysis of various sub-samples shows that in some cases it is possible. Importantly, long investors do achieve small but significant abnormal returns greater than zero in the first year of an investment, while short investors receive significantly negative abnormal returns. This pattern repeats itself when examining the returns through the full length of the investment or the current period as shown by looking at the return based on the type of individual type of activism. The figures also support previous research that has shown activism surrounding M&A has positive abnormal returns. In particular, when activists push for the sale of a company or a merger they achieve significant returns, but other types of M&A activism, such as pushing for an acquisition, opposing a merger, takeover, or acquisition, and rebuffing the terms of a deal, can lead to insignificant or negative abnormal returns.

³⁵ The results were found to be statistically significant.

Table 4: United States Follower Returns by Outcome & Sector
(Source: Bloomberg)

	Successful	Partially Successful	Unsuccessful	Compromise/Settlement Unresolved	Withdrawn Nominations	Withdrawn Demands
Basic Materials	-18.02%	-12.89%	-6.74%	-4.84%	-4.12%	17.59%
Conglomerates	30.33%	N/A	9.32%	N/A	N/A	N/A
Consumer Goods	12.40%	5.24%	14.02%	4.04%	18.46%	27.56%
Financial	14.70%	2.67%	17.43%	23.24%	8.30%	11.55%
Healthcare	27.98%	49.58%	340.38%	60.68%	68.18%	61.48%
Industrial Goods	-1.73%	22.11%	14.50%	-8.20%	16.90%	19.75%
Services	10.68%	7.14%	6.54%	6.85%	10.95%	27.83%
Technology	129.40%	16.65%	15.83%	58.76%	48.31%	19.28%
Utilities	-28.18%	N/A	2.70%	N/A	N/A	N/A
Average S&P Returns by Outcome & Sector						
	Successful	Partially Successful	Unsuccessful	Compromise/Settlement Unresolved	Withdrawn Nominations	Withdrawn Demands
Basic Materials	11.74%	12.92%	11.11%	11.93%	14.23%	21.45%
Conglomerates	8.18%	N/A	17.32%	N/A	N/A	N/A
Consumer Goods	12.52%	10.12%	11.29%	13.75%	13.31%	13.92%
Financial	11.69%	10.64%	10.00%	10.06%	14.03%	11.50%
Healthcare	11.09%	12.05%	27.74%	13.41%	12.45%	12.03%
Industrial Goods	10.78%	15.88%	15.33%	10.59%	13.46%	14.35%
Services	10.82%	9.71%	9.77%	10.38%	12.24%	13.74%
Technology	12.99%	12.48%	11.91%	15.12%	16.35%	13.89%
Utilities	7.77%	N/A	14.15%	N/A	N/A	N/A
Average BHAR by Outcome & Sector						
	Successful	Partially Successful	Unsuccessful	Compromise/Settlement Unresolved	Withdrawn Nominations	Withdrawn Demands
Basic Materials	-27.29%	-23.87%	-17.40%	-15.93%	-18.77%	-2.99%
Conglomerates	20.48%	N/A	-6.82%	N/A	N/A	#VALUE!
Consumer Goods	-0.61%	-3.22%	2.72%	-8.51%	4.55%	11.51%
Financial	2.38%	-7.36%	6.64%	11.79%	-10.10%	0.19%
Healthcare	14.44%	30.45%	163.03%/9.24%	37.62%	49.54%	44.14%
Industrial Goods	-12.75%	5.43%	-0.72%	-17.50%	2.18%	4.72%
Services	-0.49%	-3.32%	-3.17%	-3.37%	-1.69%	11.60%
Technology	107.48%/16.43%	3.54%	4.14%	31.11%	27.87%	4.27%
Utilities	-34.30%	N/A	-10.03%	N/A	N/A	N/A

Long-term Performance in the United Kingdom

In the UK, in the month prior to the announcement of activist actions the companies had average returns of 3.02%, slightly above the FTSE 100 index average return of 1.13%.³⁶ Despite relatively weak market index returns in the year following the announcement of an activist action at 5.5%, the evidence does not support the expectation that average target returns are greater than zero. Activist targets have a mean return of 12.89% in the one year post-action, with a mean return of 5.78%.

The two most popular types of activism in the UK are Board Related activism and M&A Activism. The mean annualised return to activist targets during the investment period (where the exit date is available) or at 30 June 2015 was 21.03%. Meanwhile, the mean FTSE 100 index return during the same investment period was only 0.25%, leading to a mean annualised long-term return of 23.63% for activist investors. The analysis indicates that the difference between average target and average index returns is not zero. Testing the mean return also indicates it is statistically greater than zero.

In evaluating whether activists generate positive abnormal returns the evidence shows that time is an important factor. In the first year after the announcement of an activist action, although the mean buy-and-hold returns are over 5%, the statistics do not show that they are significantly greater than zero. However, over longer time periods, when investments are measured to their exit date or the current period, the mean buy-and-hold returns increase to a point well above the market index. At such values the evidence supports the proposition that activist campaigns can improve company performance over longer time periods.

³⁶ Despite the gap, the average pre-action return of 1.95% is not supported to be statistically greater than zero.

Long-term Performance in Germany

Activist campaigns in Germany have pre-action returns in the month prior to announcement of 0.93%. During the same time periods the Deutsche Börse (DAX) average return was 1.26%. The index-adjusted return for the same period is found to be 0.57%. The sample of activist targets shows a group trading in line with the market in the month prior to a given campaign.

The post-action performance tells a different story. In the year following the announcement of an activist action the firms' average returns is 5.65%. During this time the DAX index averaged returns of 15.34%. The end result is an index-adjusted average target return of -8.52%. Like the larger sample from the United States, more than half of the German campaigns have negative post-action returns. The majority of actions involved board-related activism while several others involved M&A activism.

The average annualised return to German activist targets is 11.33%. The average annualised index return during the same investment periods is 13%. Comparing the two means indicates the difference between the two is not significantly different from zero. The index-adjusted return is -1.60%. Compared to the two other regions, the activist targets exhibit narrower trading ranges and a lower return in Germany. However, given the total sample size for campaigns against German companies, it makes it more difficult to draw comparisons between the three. In the case of Germany it is not possible to show that campaign returns are statistically greater than or less than zero, therefore the suggestion that activists can generate abnormal returns is not supported.

*Table 5: Germany Annualised Follower Returns
(Source: Bloomberg)*

Company	Price at Action	Price at 6/30/2015 or Exit Date	Trading Days	Market Price at Action	Target Gain	Market Gain	Target Return	DAX Return	Trading Period (Years)	BHAR
KHD Humboldt Wedag International AG	6.63	2.60	1010	7163	-60.79%	52.79%	-21.02%	11.28%	3.97	-29.03%
Balda AG	4.84	2.40	871	6354	-50.36%	72.24%	-18.51%	17.23%	3.42	-30.49%
Commerzbank	1.72	11.47	813	6675	568.51%	63.98%	81.30%	16.75%	3.19	55.29%
Bilfinger Berger	81.57	33.93	581	7984	-58.41%	37.08%	-31.92%	14.82%	2.28	-40.71%
Yoc AG	5.16	2.50	522	7914	-51.63%	38.30%	-29.83%	17.14%	2.05	-40.09%
GSW Immobilien AG	32.99	57.00	536	8370	72.78%	30.77%	29.66%	13.59%	2.11	14.15%
Kabel Deutschland – M&A	85.10	120.00	453	8447	41.01%	29.58%	21.31%	15.68%	1.78	4.87%
Lanxess	51.96	52.89	449	8613	1.79%	27.08%	1.01%	14.55%	1.76	-11.82%
Celesio – M&A	23.35	24.97	54	9300	6.94%	3.19%	37.20%	15.97%	0.21	18.31%
ThyssenKrupp	17.47	23.34	390	9172	33.57%	19.32%	20.80%	12.23%	1.53	7.64%
Wacker Neuson	12.35	18.80	325	9056	52.23%	20.85%	38.98%	16.00%	1.28	19.82%
SMT Scharf	19.45	16.00	308	9587	-17.74%	14.16%	-14.91%	11.57%	1.21	-23.73%
Koenig & Bauer AG	11.8	20.22	296	9402	71.31%	16.42%	58.89%	13.97%	1.16	39.42%
Sky Deutschland – M&A	6.97	6.43	133	9702	-7.73%	-4.68%	-14.28%	-8.76%	0.52	-6.05%

Data and Methodology

The aim of this report was to evaluate the effects on publicly traded companies that were targeted by shareholder activists. The methodology for doing so included a short-term event study and a long-term evaluation of buy-and-hold abnormal returns to investors. To achieve that, a list of public targets has been compiled that dates from 2010 to the present, which reflects activism in the post-financial crisis world. In addition, a review of the activists themselves is conducted. The number of engagements, tactics used, and success rates (by campaign) has been reviewed as well as returns to followers. In addition to returns, data is collected for individual targets in comparison to the most commonly used or appropriate index in order to study short-term event windows.

When performing an event window study, the goal was the look at the effect of a singular event in a short time frame. Starting with the identification of an event, a period of time (usually one or several days) was chosen to identify changes in behaviour as a result of the event. This was repeated for United States, Germany and United Kingdom, in order to be able compare and contrast the data between the regions.

To evaluate event window data, the results are broken down to show the ten-day pre-event returns, event day returns, and ten-day post-event returns. The "Action Date" is used as the event day, as this coincides with the registration of a 13d SEC filing or press release by activist investors. The Action Date is often not the same as the initial investment date. To study event returns that ten days before and after the Action date were included in the sample. The hypotheses being tested are that event returns and the post-event returns are significantly different, either greater than or less than, zero when measured against the market index.

The second section of data corresponding to activist campaigns in three countries looks at follower returns from five perspectives: by

campaign outcome, market capitalization, activist action, company response, and campaign outcome. The initial list of activist actions has been collected from Activist Insight's database of actions from 2010 to 30 June 2015. For the consistency of analysis, only companies from NYSE, NASDAQ, Deutsche Boerse and LSE were included. The sample sizes were 716, 45 and activist campaigns for US, United Kingdom and Germany respectively.

While measuring and comparing short term and long term returns on stock in the three mentioned countries, two main methods were selected: BHAR and CAR.

These models rely on calculating and comparing sample mean return and cumulative mean of abnormal returns in accordance of event timing. To increase the accuracy and ensure the reliability of the study, daily asset return data has been used rather than monthly and the results have been tested using statistical significance (in most cases, hypothesis testing and p-value). This is particularly important for evaluating long-term returns on stock.

BHAR models were used to evaluate the long term performance of the stock. These models typically compare returns for a company or portfolio against the expected returns for a matched company or portfolio of companies. The most commonly used comparative metrics are size and book-to-market ration. Ever since being championed by Benjamin Graham, using company size (market capitalization) and book-to-market equity ratio have been popular metrics for predicting stock returns.

Notes on Authors

Douglas Markey, MBA student at Cass Business School.

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Dr Valeriya Vitkova, MARC Research Fellow, who recently completed a PhD on *Topics in Mergers and Acquisitions* at Cass Business School.

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Cass Business School

In 2002, City University's Business School was renamed Sir John Cass Business School following a generous donation towards the development of its new building in Bunhill Row. The School's name is usually abbreviated to Cass Business School.

Sir John Cass's Foundation

Sir John Cass's Foundation has supported education in London since the 18th century and takes its name from its founder, Sir John Cass, who established a school in Aldgate in 1710. Born in the City of London in 1661, Sir John served as an MP for the City and was knighted in 1713.

