Everyone's a Target: Activism's Mega Year

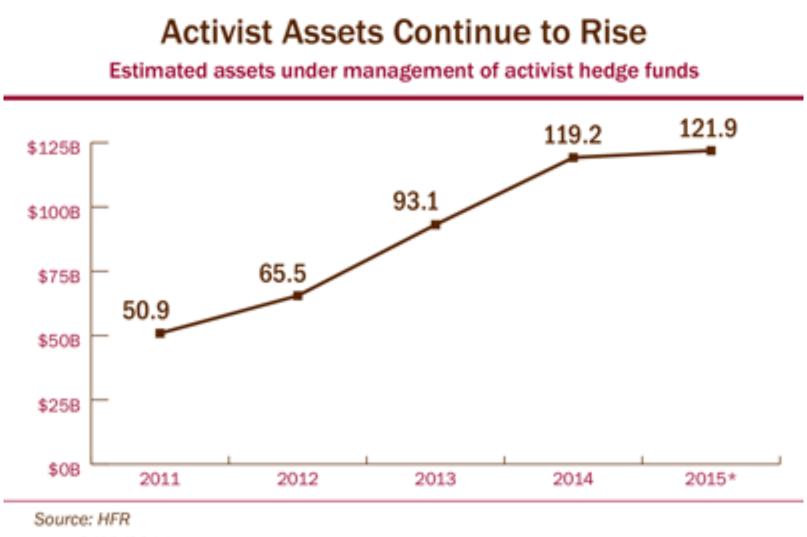
By Marc Hogan December 21, 2015

Shareholder activists took aim at their largest targets yet in 2015, a story line that reached a fittingly blockbuster-size climax this month when **Dow Chemical** and **DuPont**, both subject to activist pressure, declared a $130 billion mega-merger.

One of the biggest deals in the history of business, the pact added an exclamation point at the end of a year when activism accelerated beyond its already bustling 2014 levels. It was a year of similar activist successes. At the same time, activism defense advisors say, 2015 was marked by boards becoming more engaged with the sentiment of shareholders overall, including traditional, long-only institutional investors.

There is no letup in sight for shareholder activism, which will continue to affect companies of all sizes in 2016, these board advisors say. If the past year brought heightened director awareness of the activists at their gates, the next 12 months may see boards going beyond “thinking like an activist” to addressing their composition. Strong companies as well as troubled ones are in the cross hairs, and traditional institutions as well as activists are the ones fixing the sights.

“The biggest change in the overall behavior of boards may come not from Sarbanes-Oxley and Dodd-Frank and people interested in good governance,” says **Mark Nadler**, principal at **Nadler Advisory Services**, a board and executive consultancy firm. “It may in fact come from the influence of the marketplace making it clear to boards that they need to be doing what they should have been doing all along: thinking and acting on behalf of the shareholder.”



Size was of no consequence to activists this year. DuPont, with a market cap of more than $60 billion, was one of the largest companies ever to defend itself in a proxy battle with an activist. It defeated **Nelson Peltz** — only to change CEOs and then pursue the Dow mega-deal anyway.

Meanwhile, the $70 billion-plus **American International Group** faces a call by **Carl Icahn** to break itself into three parts.

In addition, Peltz's **Trian Fund Management** bought a stake in **General Electric**, which at more than $300 billion in market cap would be by **FactSet**'s measure the third-largest activist target, following campaigns by Icahn at **Apple** and **ValueAct Capital Management** at **Microsoft**.

Among companies with roughly $500 million or more in market cap, 160 faced a real challenge to their strategies so far this year, says **Jim Rossman**, head of corporate preparedness at **Lazard**. About 40% of those involved requests for board seats. Rossman counts 105 board seats this year that were filled due to activism. "Activists were more emboldened in 2015 to push their agenda," he says.

Given how many activist nominees are joining boards, incumbent directors may want to prepare themselves in case their boardroom is next, says **Deloitte Advisory Services** principal **Chris Ruggeri**. For example, boards may want to raise the minimum number of directors needed to call a board meeting or revisit the responsibilities for committee chairs.

"The advice that I would have given to my clients last year still stands," Ruggeri says. "The best defense is being prepared."

Activist funds still have plenty of cash in their war chests. Assets under management were almost $122 billion at the end of September, according to **HFR**. While that's up about only 2% from slightly more than $119 billion at the end of last year, it still towers over the roughly $51 billion the category held at the end of 2011.

The results of a recent survey by **FTI Consulting** and **Activist Insight** reiterate the potential for a busy 2016 for activists. Of 24 activist firms responding, more than 85% indicated they plan to enter at least three new campaigns in the next 12 months. That's in keeping with this year, when 31 activist funds targeted three or more companies, according to FTI and Activist Insight.

The types of activists boards can expect in the year ahead fall in two categories. **David Hunker**, head of activism defense at **JPMorgan**, says the top tier of activists will be delivering "more nuanced, more complex" campaigns.

"On the other end of the spectrum," Hunker says, "given all of the new entrants into this activist space, we expect to see companies that maybe don't deserve the attention of a shareholder activist getting that attention."

Bruce Goldfarb, president and CEO of proxy solicitation firm **Okapi Partners**, has also noticed the arrival of activism newbies. "We're hearing from a lot of activists, even first-time activists, who are gearing up for proxy season next year," he says.

Behind both the additional strategic options available to sophisticated activists and the chance that any company, no matter how well-run, might be a target, Lazard's Rossman cites the booming deal market. Mergers and acquisitions have totaled an annual record high of $4.6 trillion so far this year, according to **Dealogic**, with the booming market giving activists potential routes to unlocking shareholder value regardless of whether they found other faults with management's approach. "There's no wall around you," Rossman says.

Boards, too, became more sophisticated in their approach this year. More companies were willing to go all the way to a vote, not because they were blind to the activist threat but instead because they had engaged with shareholders and developed their own value-enhancement plan, says **Keith Gottfried**, head of the shareholder activism defense practice at **Morgan Lewis & Bockius**.

At the same time, where Gottfried used to say that the board of an activist target was typically fending off its first activist challenge while the activist fund was vastly more experienced, now more boards have members who have seen activists firsthand at other companies. "The companies are not as much sitting ducks as they used to be," he says.

Engagement is a major thread running through the year in activism, with Lazard's Rossman saying some directors attend "governance roadshows" held by their companies with major shareholders. But beyond outreach, activism defense advisors expect board composition will be a bigger focus for companies in 2016. "If last year the theme was [that] boards need to learn more about shareholder engagement, this year our message is going to be, 'Boards, there should be self-evaluation taking place,'" Rossman says.

As boards are forced to take a harder look within their own ranks, it may be fitting that proxy battles are predicted to become more personal, as well. "It's not just going to be a proxy contest about why their four candidates are great," JPMorgan's Hunker says of the activists. "It's going to be a proxy contest about why these four existing board members are terrible."

While that might hit a bit close to home, activism is also becoming increasingly global. **Dan Loeb**'s **Third Point** has drawn attention in Japan, while **Paul Singer**'s **Elliott Management** has been busy in South Korea. But "it's not a one-way street," says Hunker. "We are seeing some of the local non-U.S. activists start to target U.S. companies."

Activists aren't the only investors with clout in activist challenges, as highlighted by the decisive role traditional institutional investors played in DuPont's proxy contest. This month **Wachtell, Lipton, Rosen & Katz** founding partner **Martin Lipton** focused on the likes **BlackRock**, **State Street** and **Vanguard** in his annual memo outlining thoughts for boards.

"What management teams and boards need to understand is that there are no more 'company-friendly investors,'" Hunker says. "Every institutional investor is willing to support a shareholder activist if they feel that shareholder activist has a shareholder-value-enhancing idea."

As the lines blur between activists and other investors, what boards are doing to address activists more clearly overlaps with what governance advocates were calling for them to do all along. "What activism has changed is — it's really caused there to be an acceleration of time frames," Ruggeri says.

“And the debate about strategic direction, which used to be contained to the boardroom and the management team, now can be in a broader forum.”