Group report – Active Ownership

22E00500 - Corporate Governance

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1. Introduction

This report is done as a part of the Corporate Governance course at Aalto University in the fall of 2022. The purpose of this report is to analyse the concept of active ownership and to give its reader a comprehensive overview of active ownership.

1.1. Definition

Active ownership is becoming more and more relevant for both investors and companies. According to the UNPRI (2018), a United Nations-supported international network of financial institutions that promotes active ownership as a part of responsible investment, active ownership is globally one of the fastest-growing investment strategies in listed equity. In 2021, the UNPRI had over 3 800 financial institutions as signatories of its Principles for Responsible Investment, which together held over 29 trillion USD in assets under management in 2021[1]. Over 90% of its signatories engaged in dialogue on ESG (environmental, social, and governance) issues with listed equity companies in their portfolios in 2018. In 2021, activist shareholders also launched 173 public campaigns in listed companies globally according to a review by Lazard (2021). The number of campaigns decreased during the pandemic but the trend is expected to turn around this year as the number of campaigns has already grown 39% year-on-year by the end of Q3/2022 (Lazard, 2022).

Active ownership is used interchangeably with the term *shareholder activism*. The UNPRI (2018) defines active ownership as "the use of the rights and position of ownership to influence the activities or behaviour of investee companies". Goranova & Ryan (2014), in turn, define shareholder activism similarly as "actions taken by shareholders with the explicit intention of influencing corporations' policies and practices". A similar definition for shareholder activism is also used by Gillan & Starks (2007), who refer to shareholder activists as investors who are "dissatisfied with some aspect of a company's management or operations, try to bring about change within the company without a change in control". Some authors, however, define active ownership as a similar concept but with wider goals. For example, Dimson et al. (2015) define that active ownership focuses on the interests of a wider range of shareholders, such as employees, customers, and creditors,

[1] About the PRI | PRI Web Page | PRI (unpri.org)

rather than just those of the shareholders as is common in traditional shareholder activism. To avoid any confusion, we will use the term active ownership and shareholder activism interchangeably throughout this report and use them – in their wider meaning – to refer to the actions taken by shareholders to influence companies' policies and practices to serve their own or other stakeholders' interests.

1.2. Activism as a process

Active ownership can be depicted as a process as seen in the model created by Goranova & Ryan (2014) based on research synthesis (Figure 1). In the model, *antecedents* refer to firm, activist, and environmental characteristics that trigger or facilitate activism events. *Processes*, in turn, illustrate the interaction between shareholders and managers. Finally, *outcomes* describe the impact of the activism on the firm, activist, and environment.

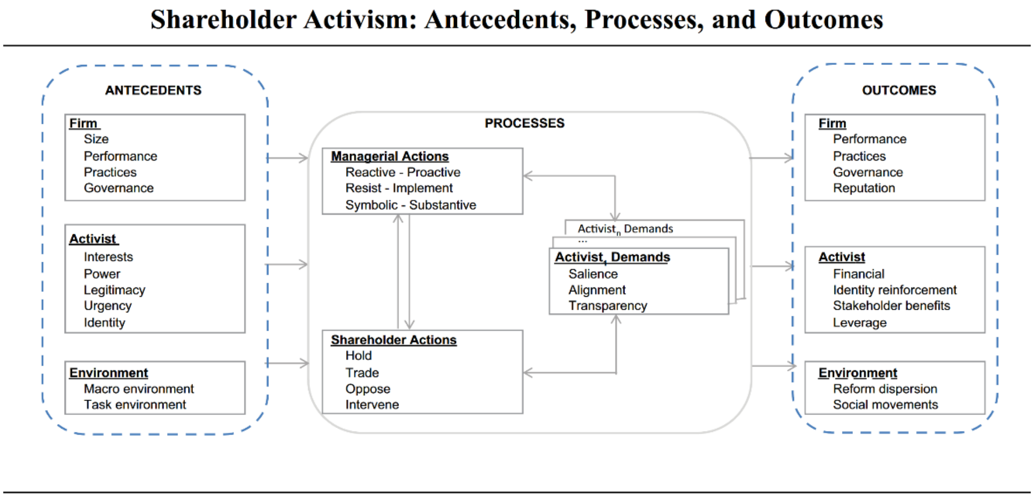

Figure 1 - Components of shareholder activism (Goranova & Ryan, 2014)

Activism, however, should not be understood as a one-time process taking place independently but rather as a self-feeding loop. For example, Connelly et al. (2010) describe ownership as an iterative form of corporate governance. They present a model that describes how influencing methods used by shareholders (incl. activism) affect firm outcomes and attributes, which in turn affect the ownership of the company, which again affects the used influencing methods by shareholders. In other words, activism taking place now will influence future activism towards the company – and to some extent towards other companies through environmental outcomes, social movements, and reform dispersion as suggested by Goranova & Ryan (2014).

In this report, we will largely follow the model by Goranova & Ryan (2014) to study active ownership and its components. Considering how many different factors affect activism and the multitude of possible actors in the field, we will only provide a short overview of the different components together with practical examples.

2. Antecedents

2.1. Motives behind activism

To understand the antecedents of shareholder activism, we must start with the interests that cause shareholders to engage in activism. In active ownership literature, *agency theory* (Jensen & Meckling, 1976) is used as the main explanation for activism. In fact, the theory is evoked five times more likely than any other framework (Goranova & Ryan, 2014). According to the agency theory, shareholder activism arises as a response to the potential gains from addressing the agency conflict between the shareholders and management (Gillan & Starks, 2007). Especially in large publicly traded companies, ownership can be dispersed and passive, resulting often in a misalignment of interests between shareholder and managers. When the agency conflict shows sufficiently big, shareholders start to address it through activism. Activists can thus be seen as expressing their dissatisfaction with corporate governance or firm performance or demanding specific actions from the management (Goranova & Ryan, 2014).

The major challenger to the agency theory is the *stakeholder theory*, which challenges the shareholders' position as the only important stakeholder of the company by highlighting the importance of considering the interests of a wider range of stakeholders (such as employees, customers, creditors, and society as a whole) (Goranova & Ryan, 2014). The reasoning is that since companies are dependent on their stakeholders, considering the interests of the stakeholders can be beneficial also for the company and its shareholders not only in terms of ethicality but also financially. The potential financial benefits are especially apparent, for example, for investors who invest widely in the market (e.g. large institutional investors) or according to an index (e.g. index funds) and thus cannot invest in a way that minimises risks from corporate externalities, leading them to take stakeholders interests into account in their activism (Dimson, et al., 2015; PwC, 2022).

In summary, shareholder activism can be split into two main forms: 1) *financial activism*, which focuses on shareholder value, and 2) *social activism*, which focuses on broader corporate outcomes and stakeholder issues. These two types of activism are not mutually exclusive and can be carried out at the same time. As mentioned above, social activism can also be financially motivated. Overall, together these two forms of activism act as a driving force for activism and affect its appearance in practice.

2.2. Target firms

Any company can be the target of shareholder activism, but some are likelier targets than others.

In line with the agency theory, activism should arise especially in companies that are underperforming as the potential gains from addressing the agency conflict are likely to be high. The underperformance could attract activism from existing investors, who are unhappy with the management, and new investors, such as hedge funds that often try to buy shares at a low price and then improve the value of the company through activism. As summarised by Goranova & Ryan (2014), many studies have found that poorly performing companies, in terms of share price and operating performance, are likelier to be targeted – although at the same time some studies have reported the relationship as insignificant. One could argue that many investors instead give up on poorly performing companies rather than engage in activism to fix them. At the same time, even well-performing companies might benefit from activism, for example, regarding future strategies.

Activism can also arise from the ESG (environmental, social, and governance) practices of the company as predicted by the stakeholder theory. For example, Dimson et al. (2015) report that companies with inferior governance and socially conscious institutional investors are more likely to face activism. One recent example of ESG activism is the campaigns initiated by shareholders of oil companies, such as Shell[2] and ExxonMobil[3], because of the companies' significant negative climate impact and unwillingness to adapt their business models. However, the list

[2] An activist investor targets Shell | The Economist
[3] ExxonMobil loses a proxy fight with green investors | The Economist

of possible triggers is long, as seen in a data set of activist sequences initiated in listed US companies between 1999-2009 gathered by Dimson, et al. (2015) (Figure 2). Dimson et al. also note that public attention plays a key role in triggering ESG activism: 46.6% of ESG engagements in the sample are preceded by public news relating to the issue.

Areas and Themes	Issues within each theme		Sequences
1. Governance			
Corporate governance	Audit and control, Board structure, Remuneration, Shareholder rights, Transparency and Performance	CG	900
2. Environment			
Climate change	Biofuels, Climate change strategy, Emissions management and reporting		156
Ecosystem services	Access to land, Biodiversity management, Water		77
Environmental management	Environmental standards, Pollution control, Product opportunities, Supply chain environmental standards, Waste / recycling		221
3. Social			
Public health	Access to medicines, HIV/AIDs, Nutrition, Product safety		31
Human rights	Community relations, Privacy and free expression, Security, Weak governance zones	ES	182
Labor standards	Diversity, Health and safety, ILO core conventions, Supply chain labor standards		225
Business ethics*	Bribery and corruption, Political influence, Responsible marketing, Whistle-blowing systems		211
Sustainability management & reporting*	Disclosure and reporting, Governance of sustainability issues, Stakeholder engagement, UNGC compliance		149
Grand total of all CG and ES themes			**1,792**

Figure 2 - Breakdown of engagement areas, themes, and issues (Dimson, et al., 2015)

2.3. Activist types

Any shareholder can be an activist. However, some types of activists are more active than others and the average activist is nowadays very different than decades ago.

History

As described by Gillan & Starks (2007), up to the 1970s most of the shareholder activists were individual investors. From the 1980s onwards there was an increase in the involvement of institutional investors, which were mainly public pension funds at the start. In the 1980s there was also an increase in corporate riders, which are described as the ultimate activists who used the market for corporate control in trying to impose discipline on boards and management. In the 1990s, new regulatory changes were introduced that enhanced the ability of shareholders to communicate on voting issues. At the time there was also a decline in the takeover market. These factors lead to a situation where institutional investors came to the fore and took an even bigger role among activists. The increase of institutional investors has continued to grow also in the 2000s. Figure 3 demonstrates that institutional investors held only about 10 % of U.S. equities in 1953, but their percentage ownership increased to over 70 % by the end of 2006.

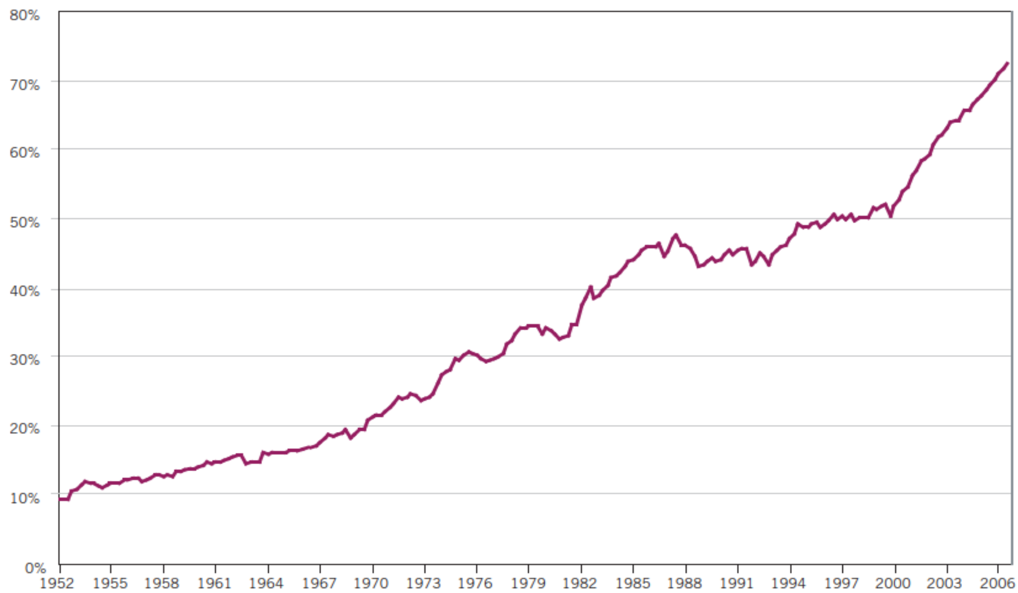

Figure 3 - Percentage ownership of institutional investors in U.S. stock markets (Gillan & Starks, 2007)

The evolution of activism continues has continued up to this date. For example, in the past few years especially hedge funds and private equity funds have assumed prominence in the shareholder activist arena. At the same time, investments into funds that apply ESG investment criteria has grown significantly: the assets under the management of these funds have tripled between 2018 and 2021 (Lazard, 2021).

Activist categories

Categorising activists is difficult because of the multitude of descriptive characteristics, such as form (private person vs legal person), interests (e.g. financial and social), resources (e.g. time, money, knowledge, skills), power (e.g. number of votes, ability to sway other shareholders, leverage), and urgency (long-term vs short-term goals). One possible classification of common types of activists is proposed by Filatotchev & Dotsenko (2015): 1) traditional institutional investors, such as pension funds and insurance companies, 2) their associations, 3) investment management companies, 4) associated companies that have business interests in the target firms, 5) hedge funds, and 6) private investors and 7) other investors such as unions, human-rights groups, and environmental groups. Below we have categorised the activists into a smaller number of groups for simplicity as described some of their characteristics.

Private investors are non-professional individuals investing in companies. Their investment strategies and interests can vary significantly. However, they typically do not hold that much power alone or do not have that many resources for activism. They can still take part in activism, for example by voting, asking questions in AGMs, making shareholder proposals, and taking part in activist campaigns.

Activist groups, such as environmental groups or human-rights groups, are distinct from other activists as they typically do not strive for financial improvement but rather for ESG outcomes. One example of such a group is As You Sow[4], which was founded already in 1992, that has as its mission “to promote environmental and social corporate responsibility through shareholder advocacy, coalition building, and innovative legal strategies”. The organisation applies a wide range of strategies, such as direct negotiations with companies, public awareness, and campaigns. The organisation might not hold many shares in companies, but it has the resources to drive campaigns and the power to sway other shareholders. For example, the or-

[4] https://www.asyousow.org/

ganisation won 98% support from General Electric shareholders in 2021 on a proposal calling for the company to issue a report on how it would reach net zero by 2050[5].

Large non-institutional shareholders, such as founders, families, and companies with business interests can hold a lot of power over a company because they can often influence the appointment of directors and directly negotiate with the company. Thus, there can be less need for indirect forms of activism, such as shareholder proposals. Many such investors also are interested in the long-term stability of their investments, e.g. to preserve the social-economic status of their family. Some examples of such shareholders are the Heineken family which holds a major share of the Heineken Group through a complicated arrangement[6] and Fortum, a Finnish energy company, that holds over 50% in Uniper, a German energy company[7].

Institutional investors, such as banks, pension funds, and investment management companies, invest money on someone else's behalf. Institutional investors typically hold a lot of funds and can hold quite many shares in a company. They also have a lot of resources available and can have very sophisticated investment and active ownership policies. For example, a Finnish bank, Nordea, has a public active ownership policy where it describes different forms of activism it applies (voting, engagement, and exclusion), the resources it applies to the management (e.g. portfolio managers, ESG specialists, financial analysts), and extensive statistics about its activity[8]. Similar policies are also published by for example Varma[9], a Finnish pension company, and Credit Suisse[10], a Swiss bank. Unsurprisingly, Goranova & Ryan (2014) report that institutional ownership has been found to be positively related with shareholder activism in research.

Hedge funds as described by the Economist[11] are "pooled pots of money that are open only to 'sophisticated' investors, and which tend to use complex strategies and

[5] https://www.reuters.com/business/sustainable-business/shareholder-advocacy-group-goes-after-environmental-racism-2021-08-11/
[6] https://www.theheinekencompany.com/investors/governance/ownership-structure
[7] https://yle.fi/uutiset/3-12579855
[8] Investments | Nordea
[9] Varma's ownership policy - Varma
[10] Active Ownership (credit-suisse.com)
[11] https://www.economist.com/the-economist-explains/2015/03/30/how-hedge-funds-work

instruments". They are characterised by high fees and high risks but potentially higher returns. They originally focused on hedge strategies, meaning that they applied both short and long positions at the same time to bet on investments and to insulate themselves from risks. Nowadays, hedge funds apply a wide range of strategies, typically focused on exploiting market mispricings. To this end, a hedge fund may buy shares in a company that it considers undervalued and then engage in activism to drive changes in the company that increase the company's value. On other hand, there are also hedge funds that make money by shorting overvalued companies. Hedge funds usually hold a significant number of shares in companies to have enough influence to bring about the necessary changes, for example, through proxy battles and direct negotiations. As a result, hedge funds are currently one of the most prominent activists on the market.

2.4. Environment

No company exists in a vacuum but rather is influenced by many factors that ultimately affect activism as well. For example, the nature of the capital markets has changed significantly in the past decades as seen in previous sections. At the same time, ESG requirements and social movements have affected companies' practices and the demands made by shareholders.

One key environmental antecedent is the prevailing legal frameworks that form the basis for activism by defining the legally enforceable influencing methods available to shareholders. In fact, the current wave of U.S. shareholder activism began with the SEC's introduction of a rule in 1942 that allowed shareholders to submit proposals for inclusion into corporate ballots (Gillan & Starks, 2007). In 1970, the foundation for social, environmental, and political activism was formed as a lawsuit ended up overruling the SEC's position that companies could block social issue proposals because they promoted actions improper for shareholder consideration (Goranova & Ryan, 2014). In the 1990s, new regulatory changes were introduced that enhanced the ability of shareholders to communicate on voting issues (Gillan & Starks, 2007). In turn, during the Trump administration proposal rights were restricted, for example by limiting them to concern only the company' business rather than general business conditions[12]. However, the rules were later largely overturned and updated.

In addition to proposals, shareholders have many other methods at their proposal, such as a voting right, the ability to demand an extra annual meeting, the right to raise lawsuits against the company and its management, the right to demand general meetings to be organised, etc. However, the legal framework for shareholder influencing methods is not uniform across countries. For example, the capital requirement to call an extraordinary meeting can range from 3% to 20% between countries (Djankov, et al., 2008). It is also worth noting that available methods and shareholder power may be restricted or increased to some extent through the company's articles of association, for example through "poison pills", different share classes, and clauses on shareholder rights. On the other hand, not all available influencing methods, such as public pressure and private negotiations, are directly specified in the law or the articles of association. Some additional examples of differences and available methods are given in Chapter 3.

In addition to the forms of activism, environmental differences also affect the prevalence of activism. A study by Becht et al. (2017) on hedge fund interventions between 2000 and 2010 revealed that activism was most prevalent in absolute numbers in the US and United Kingdom (74% of all engagements), which apply the Common Law legal framework and have advanced financial markets. On the other hand, the number of interventions relative to the number of listed companies was higher in developed countries with Non-Common Law legal systems and weaker governance – potentially because of a greater potential for improvement. Such potential also seems to attract US hedge funds, which were among the most prevalent activists also in these markets (e.g. over half of the engagements in Germany were done by US hedge funds). Finally, the authors also note that a weak rule of law (e.g. in emerging markets) seems to result in lower activism – potentially because of lower shareholder protection and other risks.

[12] New SEC guidance emboldens shareholder activists as 2022 proxy season ramps up | S&P Global Market Intelligence (spglobal.com)

3. Processes

3.1. Forms of activism

Shareholder activism can take a wide range of forms and there is debate about what actions count as activism. For example, Goranova & Ryan (2014) define that shareholder activism is driven by explicit intention rather than latent intentions implicit in ownership stakes or trading behaviour. However, they also exclude takeover actions where shareholders take over the managerial duties of the targeted companies. Gillan & Starks (2007), in turn, suggest that shareholder activism can be considered more broadly as a continuum of possible actions to corporate performance and activities. At one end, shareholders express their views of corporate performance through *passive* forms of "activism", such as trading or holding the company's shares. At the other end, investors may initiate takeovers and leveraged buyouts to drive *radical* changes, such as M&As, in the company. Between these passive and radical ends exists a wide range of possible shareholder actions. For example, Denes et al. (2016) use the following types of shareholder activism in their survey: 1) shareholder proposals, 2) private negotiations and non-proposal pressure, 3) hedge fund activism, and 4) proxy contests. The list of available methods can vary between countries due to legislative differences as seen in Section 2.4. Other important factors in the choice of methods are the involved costs and required power. Some examples of commonly applied forms of activism are listed below.

Selling shares can be considered a form of activism as it highlights the discontent of the shareholders towards the company's management. According to Gillan & Starks (2007), the stock market acts as a monitoring function that puts pressure on the board and management. Selling of shares can therefore have a disciplinary impact by increasing the probability of the CEOs and management being fired. Management compensation can also be tied to the stock price, making a lowered stock price a financial punishment for them. A somewhat similar form of activism is the exclusion from investment decisions, for example, by being left outside stock indexes or target investments because of not complying with, for example, common ESG practices. For example, the Government Pension Fund of Norway, the largest sovereign wealth fund, screens companies added to its reference index each year for ESG risks and decides whether to invest in them or not or start active ownership measures[13].

Voting is one of the most important forms of activism. Most major decisions, such as electing the board and deciding their compensation, changes in bylaws, and approving financial statements, require the support of the shareholders. By voting, shareholders can express their voices and even show dissatisfaction by voting against proposals done by the board. Sometimes shareholders can organise a campaign to vote against the board or withhold support in so-called “vote no campaigns” (PwC, 2022). Many institutional investors, such as Nordea[14], also publish their voting activity as a part of their active ownership policy.

Shareholder proposals are a common way to influence a company’s decision-making. In the US, shareholders can submit proposals according to the Securities and Exchange Commission (SEC) rule 14a-8, which are then shared with other shareholders in a proxy statement ahead of the annual meeting. Shareholders can vote on the proposal, but they are in most cases non-binding, meaning that the management is not required to implement them. A somewhat similar rule is in place in Finland, where the 5 § of chapter 5 of Osakeyhtiölaki (2006/624) allows shareholders to submit proposals to the annual meeting. However, these proposals can only concern decisions that can be made by the annual meeting, i.e., the proposals cannot concern decisions for which the board and management are responsible by law.

Private negotiations are a way for the shareholders to directly deliver their message to the board and management. It can often be in the interest of the board and management to negotiate with such shareholders because the shareholders could ultimately replace them in the annual meeting if their voices are not heard. Holding the negotiations in private can have benefits, such as avoiding negative publicity or the ability to share confidential information to some extent. One recent example of private negotiations is the participation of the Finnish government as a majority shareholder in the decision-making of Fortum[15].

[13] Norway’s $1.3tn oil fund broadens ESG screening to smaller companies | Financial Times (ft.com)
[14] Voting | Nordea

[15] Tämä tiedetään pääministeri Marinin roolissa Uniper-kriisin selvittämisessä: Lähetti liittokansleri Scholzille tekstiviestejä - Politiikka | HS.fi

Public negotiations or non-proposal pressure are a way to put pressure on the company. For example, shareholders could ask difficult questions from the board in the annual meeting, publish open letters, or criticise the board and management in the media.

Proxy contests, as described by PwC (2022), are an "attempt to replace some or all of a company's board with directors nominated by the shareholder activist" and are typically carried out by hedge funds. They often involve significant costs and take a long time. Thus, companies and activists often aim for a settlement rather than engaging in a battle. In 2021, 92% of won proxy fights ended in a settlement (Lazard, 2021).

Takeovers are an extreme form of activism. A shareholder or a group of shareholders may decide to buy a significant share of the company to change its course. Perhaps the most recent example of an "activist" takeover is the purchase of Twitter by Elon Musk[16]. In the US, takeovers are sometimes hindered with "poison pills" that limit the ability to concentrate ownership beyond certain thresholds e.g. by allowing other shareholders to buy shares after one shareholder reaches the threshold (Becht, et al., 2009). Poison pills are not that common in Europe. For example, in Finland, a shareholder, who reaches 30% or 50% of votes, must make an open offer to buy the rest of the shares of the company (11 § of chapter 11 of Arvopaperimarkkinalaki 2012/746).

4. Outcomes - Case examples on hedge funds

The fundamental question about shareholder activism is whether it creates value (Denes, et al., 2016). As activism involves costs, i.e. time and resources, its benefits must exceed its costs. The shareholder activist also incurs all the costs related to activism – unless supported by other investors – while all the possible benefits of activism are usually enjoyed by all shareholders. Thus, small shareholders are likelier to favour low-cost forms of activism, such as voting or shareholder proposal, instead of resource-intensive activities, such as proxy fights.

[16] Elon Musk buys Twitter at last | The Economist

The success of activism is also uncertain. Activism may not lead to any changes in the company. The management might simply ignore or resist the demands made by the activist, for example, if the demands are not aligned with the management's views or if the voice of the activist is weak. Even if the demands are answered, there is no guarantee that they will lead to better outcomes for the company, activists, or the environment.

We will next present two different cases on hedge funds to understand how value creation works in practice and offer a summary of relevant research.

4.1. Case 1: Lindex and Cevian Capital

Our first case example illustrates a more traditional example of shareholder activism via strong operational involvement with financial interests as a goal. In 2003, a Stockholm-based activist fund, Cevian Capital, chose a Swedish clothing retailer, Lindex, as a target investment for restructuring[17]. Nowadays, Cevian Capital is considered one of the biggest activist investment firms in the world, however, at the time, Lindex was their first "big" investment.

In Cevians's opinion, Lindex was undervalued by the markets in 2003 due to a failed market entry in Germany and an unstable profitability history. Before buying a share in the company, Cevian Capital completed comprehensive background research including interviews and store visits and an operational comparison with H&M, which was successful in the same industry at the time. Eventually, their team identified several strategic opportunities and decided to buy around 10% of Lindex, becoming the largest shareholder. In 2005, the holding was raised further to 16%.

After becoming the largest shareholder, Cevian Capital restructured the board of directors and the senior management of Lindex. The founder of Cevian became the chairman of the board and the co-founder was appointed as a non-executive director. They also nominated four new board members from the industry and in addition to hiring a new CEO from H&M. In addition, option-based compensation was introduced to senior managers.

[17] Cevian Capital · The Hedge Fund Journal

Cevian also implemented several operational improvements such as improvements in inventory management, reporting, and purchasing. In addition, they decided to close 11 loss-making stores in Germany and sold one Swedish subsidiary. A new store-opening program was also released in growth markets, and they also decided to pay special dividends to the shareholders.

Operational improvements, board nominations and, for example, the announcement of special dividends, all had a positive impact on the stock price. Eventually in 2006, after three years, Cevian sold its position and achieved an abnormal return of 85%. The case is an excellent example of the potential financial benefits of active ownership implemented through effective operational improvements, changes in board representation, and intensive engagement.

4.2. Case 2: Exxon Mobile and Engine No.1

The second case is a more recent one and includes ESG issues with a clear approach to climate-related goals. In December 2020, a small activist hedge fund, called Engine No 1. launched Reenergize Exxon campaign to reduce Exxon's carbon footprint[18,19]. Three primary asks for one of the biggest oil companies in the world included:

1. Refresh the Board of Directors with energy experience.
2. Impose greater long-term capital allocation discipline.
3. Implement a strategic plan for sustainable value creation in a decarbonizing world.

Engine No. 1 held only 0.02 % of Exxon's shares, so their ability to influence, for example, the board nomination of Exxon was marginal. However, they were able to convince some of the largest institutional investors of Exxon, including BlackRock, Vanguard, and State Street. In the annual general meeting of 2021, the institutional investors combined their votes with Engine No 1. resulting in over 20% of the votes. It is not common that institutional investors to align with small operators such as Engine No 1. When looking at the campaign afterwards, Engine No 1.

[18] Exxon Mobil Defeated by Activist Investor Engine No. 1 - The New York Times (nytimes.com)
[19] Exxon Mobil One Year Later | Engine No. 1 (engine1.com)

used a skillful strategy to combine climate-related goals with increased shareholder value. They, for example, sent an 82-page pitch to other investors to explain their approach and goals regarding climate issues and to convince them of how they will also improve shareholder value.

As a result, three of Engine No. 1´s candidates were elected to the board, including a Finnish citizen, Kaisa Hietala. Also, multiple actions and strategy work has been done to reduce Exxon's emissions footprint during the past year. All of the actions were also followed by a major positive impact on the stock price. For example, the stock price of Exxon Mobil went up 45% after the selection of the board of directors compared to the beginning of the activism campaign in December 2020.

4.3. Summary of effectiveness and most effective practises

There are controversial opinions on the effectiveness of shareholder activism. To some shareholder activism holds the promise of monitoring and solving problems in widely held companies, thereby improving corporate performance (Black, 1992). However, some argue that shareholder activists lack the skills and experience to second-guess the firm’s management. As a result, activism is described as disruptive, opportunistic, misguided, and ineffective (Becht, et al., 2009).

The effectiveness of shareholder activism depends on the activists’ resources and the tools they are using. Usually, activism that mimics political democracy - such as shareholder proposals - is associated with minimal impact, whereas activism that is undemocratic in its explicit concentration of shareholdings is associated with significant improvements in the target company’s value and performance (Denes, et al., 2016). For example, Becht et al. (2009) reported in their paper substantial effects and benefits associated with shareholder activism done with private engagements by activist funds.

Boyson et al. (2016) found a positive relationship between activist experience and target companies’ CARs (bidder stock valuation effects) and long-term operating performance. The target company’s performance was optimal when experienced activists implemented shareholder activism through activist strategies, for example choosing more liquid stocks. According to the authors, hedge funds that go on to become serial activists outperform other activists. However, there are also examples of how individual investors have influenced companies successfully for example by combining forces in voting.

In comparison to financial activism, social activism has received much less attention and research in the area is also still focused on financial outcomes. Studies, such as by Dimson et al. (2015) and Barko et al. (2022), report positive abnormal returns for shareholders from successful ESG engagements. The success of engagements is likelier with firms that are concerned about their reputation and have the resources to carry out the demanded changes. The impact on society is, however, given even less attention. Barko et al. (2022) at least report that compliance with activist demands results in higher ESG ratings for companies with poor ESG ratings and lower ones for companies with good ratings as a result of revealing poor practices. However, more attention should be paid to the societal impact of activism in future research.

Our case examples reflect the general research findings. Both presented case examples led to increased short-term shareholder value, although by completely different methods. In the first example, Cevian Capital was able to raise the stock price of Lindex through effective operational improvements with intensive engagement and board work. In their own words, Cevian describes itself as an operational activist fund which also explains its influencing methods.According to Cevian, it differs from so-called mass activist funds. For example, they have a better ability to have realistic views on what is attainable operationally and strategically. In addition to its ability to change the board and management, Cevian also emphasises its extensive management and boardroom expertise. On the other hand, their strong engagement on the operational level also serves as a protection for their investment. When considering the above-mentioned characteristics, it is easy to conclude that Cevian Capital, as an activist owner, was able to achieve an extensively positive financial outcome with the help of their professionalism and exceptional overall skills in running the business.

In turn, Engine No. 1 is a great example of an activist owner who needs support from other larger owners to make an impact in the target company. It is never an easy task to get big institutional investors to align with smaller actors. However, Engine No 1. was clever in their communication, they were able to convince major institutional owners by providing them with a story which aligned with their goals as well. For example, Engine No 1. sent an 82-page pitch for every major shareholder in which they emphasised their climate agenda but also described the agenda's positive relation to the shareholder value. In other words, Engine No.1 understood, that in order to achieve their climate-related goals, they had to be able to explain why this would be an excellent agenda also for the large institutional owners.

Overall, impactful shareholder activism requires the consideration of many factors, such as the choice of the target company, timing, strategy (incl. influencing methods, demands, and goals), environmental factors (e.g. the legal framework and articles of association), and sufficient resources (time, money, and skills) and power.

5. Summary and future outlook

As described in the report, active ownership is a vast research area composed of many components and actors. Its role in the financial markets has grown over the years due to developments in legislation, financial markets, and social movements. At the same time, the emphasis on social activism has grown significantly and will continue to grow in the future. The impact of activism on the company and shareholder value is debated although some studies and case examples suggest a potential for creating value. Impactful activism, however, requires the consideration of many factors and sufficient resources and power. In comparison to financial activism, the impact of social activism on ESG factors and society remains quite understudied and researchers should focus on it in future research.

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