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Activist investors learn to mind their manners

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Investors are realising they can have more success outside the US by taking a different approach



Activist investors, from left: Daniel Loeb, Jeff Ubben and Paul Singer

It is enough to flummox the most advanced student of stylometry; enough, even, to confound a computer programmed with the latest algorithm for textual analysis.

Daniel Loeb used to lace his letters to chief executives with poison, lambasting one for having “feasted on organic delicacies and imbibed vintage wines at a cost to shareholders of multiple hundreds of thousands of dollars”, while suggesting another be “shown the door . . . accompanied by a well worn boot planted in the backside”.

So surely this is not the same Daniel Loeb who this week wrote to the management at his latest investment, in the medical supplies company Baxter International, to praise their “immense focus and detailed execution”? The hedge fund manager wants two seats for his fund on Baxter’s board, and a say in the hiring of the company’s new chief executive, and he has calculated he is much more likely to get what he wants by playing nice.

Mr Loeb's softer tone reflects an evolution among the American hedge fund managers who pioneered activist investing but whose new, civilised mien is winning them more corporate battles in the US than they ever did with poison pen letters.

It has also meant that their activism is more easily exportable, more pliable and better able to go with the grain of investment in the countries of Asia and Europe.

Change of approach

In the past 10 days, the San Francisco-based fund ValueAct — run by Jeff Ubben, one of the few activists who always made it a point not to speak ill of a management in public — has been more or less openly welcomed on to the shareholder register by the boards of Rolls-Royce and the UK's Smiths Group.

Meanwhile, activist campaigns are on the rise in Asia, especially in Japan but in China, too. After years being bellicose but trapped at the US border, American hedge fund managers have found that politeness is helping them make strides across the globe.

Mr Loeb surprised the sceptics with his success in prodding one of Japan's most reclusive companies to open up to shareholders. In February, Third Point — Mr Loeb's hedge fund — disclosed a stake in robot maker Fanuc, urging it to make better use of its cash pile. Two months later, the company, long known for shunning dialogue with investors, promised to double its dividend payout ratio and set up a new division to engage with shareholders.

So when Mr Loeb disclosed a new stake in Suzuki Motor earlier this week, the news alone was enough to boost the company's shares to a record high. The expectation is that he will be successful in persuading the motorcycle maker to further unlock value.

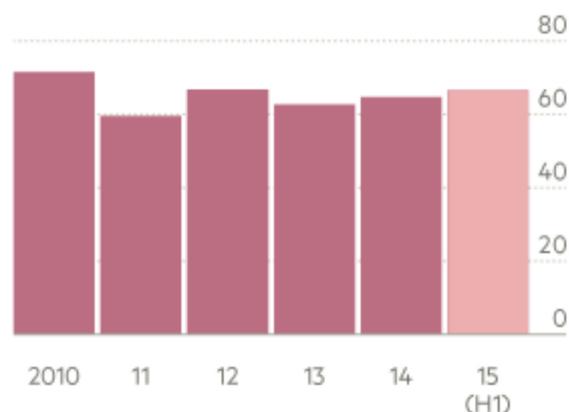
This is in contrast to the situation at Sony where, in 2013, the company refused Mr Loeb's suggestion it break itself up, after he had approached with more aggressive language. (He had described himself as "perplexed" that the company was not more concerned its movie studio had "just released 2013's versions of [box-office flops] *Waterworld* and *Ishtar* back-to-back".)

"You do need to foster cultural awareness into your campaign because you want support from local investors as well as the international ones," says Bruce Goldfarb, founder of Okapi Partners, an adviser to activists.

Mr Loeb's gentle approach contrasts with that of Elliott Management, run by Paul Singer, which has a mixed record in Asia. Using US-style tactics, including critical public letters, it aimed to undermine the chaebol system in South Korea but failed to persuade local shareholders to

Global activist success rate

Per cent



Source: Activist Insight

FT

block the acquisition of [Samsung C&T](#) by family controlled affiliate [Cheil Industries](#), which it said was an unfair deal aimed at shoring up family control. Defeated, it sold its position in Samsung C&T this week.

In Europe, however, Elliott has emphasised how its London-based activist division is run autonomously from the New York headquarters, and it has been better at adopting the consensual tone of indigenous European activists. It managed to pull off an unexpected victory in a campaign to reform the UK investment company [Alliance Trust](#), calling not for the resignation of chief executive Katherine Garrett-Cox but merely for new board members to keep a closer eye on her performance.

Mr Loeb's approach to Baxter and Mr Ubben's to Rolls-Royce and Smiths Group have been timed to coincide with changes in the C-suite, an opportune moment to argue for new ideas. ValueAct, whose previous work included a very gentle behind the scenes effort to ease out Steve Ballmer as chief executive at [Microsoft](#), has cast itself as an ally for Warren East, the new chief executive at Rolls-Royce, as he hunts for cost cuts and other operational improvements at its core aero engines division.



417

Number of companies subjected to activist demands globally in 2014

66.5%

Of activist demands were at least partially successful in the first half of 2015

Activists are learning how best to win over their real audience: the institutional investors whose large stakes, through mutual and index funds, make them in effect the deciding votes in any dispute over corporate strategy.

In the US, this has meant imbibing, at least in part, these investors' consensual approach to getting change. Many US activists now couch their demands as asking boards to "consider" spin offs and to appoint "independent" directors — rather than the activist himself — to the board. This sits well with other shareholders, who tend to believe that conflict in the boardroom has a negative effect on a company's performance.

The character of institutional shareholders differs from country to country and they do not always view their role as judging between different strategies. In the US, they have largely viewed the question of corporate structure and capital allocation to be ones for management; UK institutions tend to be more opinionated when talking to management, continental European and Asian investors less so.

Short-term thinking

Those global fund managers have not swallowed the whole activist playbook. When Carl Icahn demanded Apple immediately return \$50bn of cash to its shareholders, BlackRock and others publicly told the old corporate raider to hush his mouth. (Apple in the end promised to give back much more than that, but on its own timetable.)

Meanwhile, BlackRock chief executive Larry Fink has warned that short-term activism, designed to get a one-off share price pop from a buyback or takeover, might not be best for long-term shareholders.

Everyone seems to be headed towards meeting in the middle, however. Big US investors such as BlackRock and Vanguard have demanded more input into corporate governance and sometimes strategy, and the globalisation of the investment world will only push that trend, says Okapi's Mr Goldfarb.

“The increasingly global investor base of many non-US corporations means you have a shareholder base that may be more sympathetic to activism,” he says.

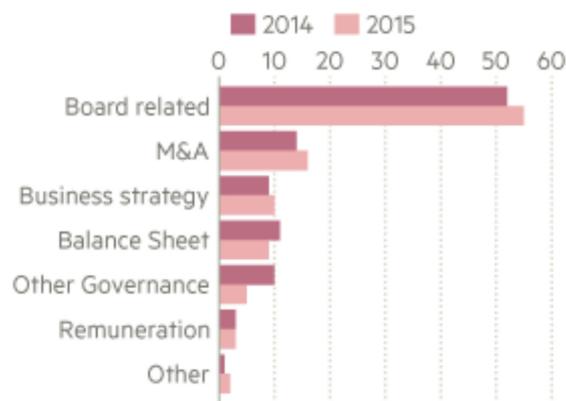
An open question is how far US activists' geographical ambitions will spread.

Many hedge fund managers have chosen to continue focusing their firepower on targets within the US. Bill Ackman — who this week revealed a 7.5 per cent stake in Mondelez, the maker of Cadbury's chocolate and Trident gum — tells investors that he sees ample opportunities in the US to keep him occupied. His fund has spent no significant effort looking for European targets.

There is a home-field advantage: the legal and corporate governance rules, whose minutiae activists exploit, are different across countries; outside the US they do not necessarily have relationships with the institutional investors they need to persuade to back them; and they risk a xenophobic backlash against overseas “vultures” such as the one that scuppered Elliott in Samsung C&T.

More board, less governance

Global activist demands (H1, %)



Source: Activist Insight



21	216
Number of Asian and European companies targeted by US activists in 2015 – Including Rolls Royce (above)	Number of US companies which have been subjected to activist demands in 2015

But weight of money suggests activists may seek more opportunities outside their home market, since there is more competition domestically. And at some point the US stock market is going to turn down, and geographical diversification could help offset that headwind.

Gary Weiss, a vice-chairman at JPMorgan Chase, says: “There is about \$130bn that is branded as activist funds, and if you add to that figure the multi-strategy funds that also engage in activism, the total amount of money potentially operating under the activist banner rises to about \$350bn. Most of these funds originate and operate in the US, and the market there has become very competitive. For that reason, we have

thought for a while that it was only a matter of time before activism spreads to Europe.”

Exporting activism

Activists are also finding the door at least half ajar in other jurisdictions — and sometimes wide open.

As part of the Abenomics project, Japanese companies are being encouraged to deliver higher returns on equity, to be more efficient in their allocation of capital, and to embrace international governance norms that could help attract foreign investment. Fanuc insists its move was in response to the country’s corporate governance reform and not the result of Mr Loeb’s prodding.

“In the past, foreign funds were seen as Matthew Perry’s black ships [which brought gunboat diplomacy to 19th-century Japan]. But that perception has changed among Japanese companies,” says Nobuhiko Hibara, associate professor of finance at Waseda Business School.

Mr Loeb has been at pains to avoid being seen as a foreign interloper, seeking out meetings with government officials of all levels, and even securing an audience with Shinzo Abe in April, as the prime minister worked to persuade foreign investors to embrace Japan.

From poison penman to prime ministerial guest — few readers of Mr Loeb’s early letters would have guessed how far he would come in a decade, the question now is how far will US activists’ newfound politeness take them.

Additional reporting Miles Johnson

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