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Shareholder Activism in the UK: Types of Activists, Forms of Activism, and Their Impact on a Target's Performance

Igor Filatotchev

Sir John Cass Business School

City University London

106 Bunhill Row

London EC1Y 8TZ

Tel: +44(0)20 7040 5278

Fax: +44(0)20 7040 8328

Email: Igor.Filatotchev@city.ac.uk

Oksana Dotsenko

Ernest & Young Ltd

Email: oksana.dotsenko@yahoo.com

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Abstract

Considering the recent rapid expansion of shareholder activism phenomenon in the United Kingdom (UK) and the vast amount of resources committed to it by corporations, government and investors, its effectiveness has become a crucial subject for investigation. This article analyzes organizational outcomes of shareholder activism in the UK. This research is based on a unique comprehensive database of shareholder activism events during the period of 1998 – 2008. We provide a detailed account of different types of activists, activism strategies and shareholder demands associated with the events of activism. Our findings show that the effectiveness of shareholder activism in terms of abnormal stock-market returns varies dramatically depending on its form, type of investor and the nature of investor proposals.

Keywords: shareholders; activism; abnormal returns

Introduction

Shareholder activism has now become a broadly used investment strategy associated with the increasing willingness of investors to trigger corporate change and intervene in management's decisions. More proactive activist approach of traditional institutional shareholders and growing role of hedge funds and international investors facilitate and reshape the development of shareholder activism. Since 1986 the number of shareholder proposals filled in the US was constantly increasing, and in 2006 it hit the record high of 645 shareholder proposals presented at the annual meetings (IRRC, 2006). In the UK, the list of companies challenged by activists recently included Vodafone, Sainsbury's, HSBC, and Tesco signalling that the size of the firm is no longer a barrier to activism. There is a continuing pressure from the government and investor associations to promote shareholder activism. For example, having introduced the 2006 Companies Act and a series of best practice recommendations, such as the Combined Code on Corporate Governance and the recently adopted Stewardship Code that targets institutional investors, the UK government provided shareholders with further capabilities to engage with companies in their investment portfolio.

Bearing in mind substantial resources committed to shareholder activism by corporations and investors, its effectiveness has become an important subject for practitioners and academics. Will the company value improve if activist shareholders make their voices heard in the boardroom? The answer to this question is very important not only to the company's long term investors but also to a wider body of stakeholders including employees and the regulator.

Despite of the increasing importance of shareholder activism, many prior studies suggests that it has minimal or zero impact on the company's share performance (Gillan and Starks, 2007; Karpoff, 2001). However, a vast majority of studies have explored only the governance effects of a single form of shareholder activism (for example, shareholder proposals or private negotiations). In addition, most of the previous studies have focused on companies and investors in the US. Institutional and legal environments may also have a significant impact on investor activism outcomes, and studying the effects of shareholder activism outside the US may enrich our understanding of this phenomenon (Filatotchev, Jackson and Nakajima, 2013).

This paper provides a detailed analysis of investor activism in the UK by looking at types of active investors, their demands and outcomes of the events associated with investor activism in terms of the short and medium term stock-market responses. It makes several major contributions to the literature. First, it provides a longitudinal evidence on shareholder activism in the UK using data for the period of 1998 – 2008. Second, we differentiate between two forms of activism: shareholder proposals and public announcements and campaigns. Although public campaigns have generated a widespread interest, there is very little evidence on their drivers or outcomes, and this study examines this form of activism separately and in comparison with shareholder proposals. Third, we extend previous studies by differentiating among different types of activist investors, as well as different forms of their demands. These differences between various forms and aspects of activism in terms of their effects on the target company imply that activist investors may have to reassess their agenda of engagement with the investee companies and use their resources more effectively focusing on the value creating forms of activism. Although this study investigates the effects on investor activism in the UK, our findings may have important policy implications for other countries, such as the US, where the level of investor activism is particularly high.

Theoretical background

A growing number of studies in economics, business strategy and corporate finance research are focused on the governance roles of large-block holders in general, and institutional investors in particular, in large, publicly traded firms (see Cunat, Gine and Guadalupe, 2012; Ramadorai, 2010, for recent reviews). This research suggests that large-block outside ownership may be an effective counter-balance to managerial opportunism. Companies may have active shareholders that play a critical leadership and monitoring role. They have both the incentives and the means to restrain self-serving behaviour of managers (Maug 1998; Zeckhauser and Pound 1990). Hoskisson et al. (2002) and Tihaniy et al. (2003) provide an extensive survey of literature which suggests that institutional investors with significant ownership positions have both the incentives to monitor executives and the influence to bring about change they feel will be beneficial. These investors use their power through the increased shareholder activism, because this strategy is a preferable modus operandi for large shareholders bearing in mind the size of their major stakes in corporations. The barriers to these investors' divestments of their holdings are high, and they have few options for alternative (large) investments (Agrawal and Knoeber 1996).

Because activist investors have both the incentive and influence to engage in shareholder activism that makes sure that managers and directors operate in the interests of shareholders, their presence among the firm's investors provides an important driver of 'good' corporate governance that should lead to efficiency gains and improvement in performance (Daily et al. 2003; Shleifer and Vishny 1997). Strategic management provides another important stream of research that links investor activism with the firm's strategic decisions. For example, using structural equation modelling, Hoskisson et al. (1994) show that large block shareholders help mitigate against poor strategy, such as diversification, to evolve into poor performance, therefore decreasing the magnitude of restructuring. Hill and Snell (1988) find that institutional ownership is positively correlated with R&D expenditures, specialization and relatedness in a sample of 94 firms in research-intensive industries.

A number of recent studies have moved from traditional empirical analysis of links between ownership structure and types of owners to more qualitative, multi-disciplinary research on actual actions of owners in terms of their involvement in corporate governance. For example, Anson, White and Ho (2004) and Daily et al. (2003) discuss corporate governance practices of large public pension funds such as CalPERS and TIAA-CREF in the USA. CalPERS, for example, has been active in seeking greater board independence by requesting that firms in which the fund invests (1) compose their boards predominantly of independent directors, (2) identify a lead director to assist the board chair, and (3) impose age limits on directors (Nesbitt, 1994). Similarly, TIAA-CREF was very critical of firms that maintain what the fund views as inappropriate corporate governance structures. Sundaramurthy and Lewis (2003) provide evidence which suggests that by publicly criticizing board oversight and confronting complacent management institutional investors destabilize managerial power and pressure strategic changes in line with shareholder demands. Black (1992) notes that institutional investors have the motivation to discourage conglomerate acquisitions that may dilute managerial attention and depress firm value. Aguilera (2005) indicates that companies in the UK and USA are under pressure from institutional investors to appoint a lead (senior) independent director whose responsibility is to serve as a communication channel between shareholders and the board.

Sundaramurthy and Lewis (2003) suggest that investor activists also act as an agent or catalyst for certain types of change. For example, they may alter the balance of power by influencing board and management turnover enabling an efficient succession (Denis and Sarin 1999). Wahal (1996) suggests that target firms are increasingly adopting proxy proposals regarding changes in corporate governance. Activist investors may initiate revisions in executive compensation (Denis et al. 1997) and in directors' term of office (Sundaramurthy and Lewis 2003).

Finally, the legal perspective on corporate governance suggests further that to be effective, institutional investors should have a right to sue directors and auditors for negligence and breach of duty (Filatotchev et al., 2013; Bethel and Gillan, 2002). In the past, the company itself primarily initiated legal actions against directors. Legal scholars suggest that shareholders should have a statutory right to bring an action enforcing the company's rights against directors through so-called derivative claims (Bebchuk, 1994; 2007). Some researchers document that the increase in shareholder activism has been accompanied by an increase in shareholder lawsuits (Kesner and Johnson 1990). Langevoort (2001) suggests that the very threat of lawsuits may provide a powerful governance effect associated with large-block shareholders. Bebchuk (1999) indicates, however, that only a small fraction of public companies in the USA faced contested board elections that were designed to oust existing directors. One of the barriers to contested board elections is associated with financial and organisational difficulties shareholders face when trying to place their own directors on a company's proxy statement.

Despite the development of shareholder activism and generally positive assessment of its governance roles by researchers, the majority of empirical studies focused on actual actions of shareholders indicate that activism has little or no effect on targeted firms (Filatotchev et al., 2007). Jensen (1993) has questioned the promise of shareholder activism in general, and institutional investor activism in particular. Their increasing reliance on indexing investment strategies suggests that they believe that, on average, their portfolio of firms will yield returns comparable to those for the market as a whole, regardless of the governance structure of their portfolio firms. Black (1992) documents an increasing importance of "exit" strategies for the fund managers as opposed to shareholder activism. Daily et al. (2003) also suggest that shareholder activism can be much more costly than pure reliance on indexing strategies.

A vast majority of empirical studies that focus on submitted shareholder proposals do not found any significant abnormal returns around the date of information release (Carleton, Nelson, and Weisbach, 1998; Gillan and Starks, 2000; Karpoff, Malatesta and Walkling, 1996; Prevost and Rao, 2000; Smith, 1996). Karpoff et al. (1996) argues that in the US most efforts of the activists seek governance changes and have negligible effects on the target company's operations or efficiency. Some studies, however, identify significant responses by looking at other types of activism events. For example, Gillan and Starks (2000) find negative abnormal returns for proposals to rescind poison pills, while Del Guercio and Hawkins (1999) report negative abnormal returns for board-related and anti-takeover proposals. Carleton, Nelson, and Weisbach (1998) suggest that market response is negative for proposals related to board diversity. Strickland, Wiles and Zenner (1996) in their study of negotiated settlements with the target company find that this kind of activism is associated with significantly positive returns. Gillan (1995), Del Guercio and Hawkins (1999) and Wahal (1996) found no evidence of significant effects on stock performance of the companies that experienced targeting for the first time. Prevost and Rao (2000) report significantly negative short term stock returns for companies targeted by CalPERS and other public pension funds. A vast majority of studies of long-term operating performance have reported no statistically significant changes in targeted companies (Del Guercio and Hawkins, 1999; Karpoff, Malatesta and Walkling, 1996; Smith, 1996; Strickland, Wiles and Zenner, 1996; Wahal, 1996).

Bearing in mind these empirical and theoretical arguments against shareholder activism hypotheses, a growing number of studies point out that the answer may be in the types of investors and what they actually do in terms of engaging with firms in which they invest. Most research on performance effects of large-block share ownership has not differentiated among types of investors. Only recently have studies acknowledged that the identity of such owners has important organisational implications because different owners may have different objectives and decision-making horizons (Hoskisson et al. 2002; Siegel, Wright and Filatotchev, 2011; Tihanyi et al. 2003). Some authors (e.g., Brickeley et al., 1988; David, Kochhar and Levitas, 1998) differentiate between "pressure-resistant", "pressure-sensitive" and "pressure-indeterminate" institutional investors. Pressure-resistant institutions, such as public pension funds, mutual funds, foundations and endowments, are unlikely to have strong business links with their investors, and they may have stronger influence on strategy choices and their performance outcomes (Hoskisson et al., 2002). Johnson and Greening (1999) also indicate that pension and investment fund managers' objective is a high relative performance of their portfolio firms because of their own reward system. On the other hand, "pressure-sensitive" investors such as insurance companies are likely to have business relationships with the firms in which they invest (Kochar and David, 1996). Because they often have an obligation to support the management's agenda, their governance role tends to be more passive compared to "activist" investors (Tihaniy et al. 2003). Corporate pension funds typify the pressure indeterminate institutional investor category. Relationship between the funds and the firms in which they invest may exist, and they are unlikely to actively challenge firm decision makers (Dalton et al. 2003).

Daily et al. (2003) and other authors suggest that only pressure-resistant investors behave in line with the assumptions of agency arguments related to the governance roles of activist investors. Georgen, Renneboog and Zhang (2008) and Faccio and Lasfer (2000) argued that some institutional investors may not intervene with their portfolio companies because of lack of monitoring expertise and the desire to maintain the liquidity of their investments as insider trading regulation prevents them from rebalancing their portfolios. Hendry and

Sanderson (2004) analyze a number of institutions including wholesale and retail asset management companies, pension funds and the investment arms of life assurance companies in the UK. The authors split their sample into 'active' and 'passive' investors according to their approach to engagement. Active investors were mainly fund management arms of global investment banks, whereas fund management arms of large life insurance companies and large self-managed pension funds were classified as passive.

Among "pressure-resistant" investors, hedge funds have gained a prominent role in the context of investor activism. Their strategy, however, is argued to differ from activism by traditional institutional investors. It is usually aimed at significant changes in specific companies, in contrast with institutional investors whose activities are often directed at changes in corporate governance rules related to a group of portfolio companies (Kahan and Rock, 2007). Several studies investigate recent trends of investor activism by hedge funds. Their results indicate that there are short-term gains associated with hedge fund activism. For example, Klein and Zur (2006) and Brav, Jiang, Portnoy and Thomas (2006) in their studies of 13D filings by hedge funds report substantial abnormal returns. Clifford (2007) suggests that firms that are targeted by hedge funds experience an improvement in operating performance and earn larger excess returns than a control group.

Finally, the vast majority of studies of investor activism reviewed in this section are focused on the US whereas the UK practices are relatively under-researched. Becht et al. (2009) study private engagements with target companies by one activist shareholder, Hermes UK Focus Fund. They report that the fund frequently seeks significant changes in the company's strategy by predominantly conducting 'behind the scene' interventions. Using the event study methodology these authors find positive short term abnormal returns on the announcement of various corporate changes that were associated with this type of engagement. However, news about fund accumulating a 3% stake in the firms are followed by a negative market response. Obviously, this research is based on a single case study and its results cannot be generalised to other shareholder activists. Moreover, it tests the effectiveness of shareholder activism in the form of private engagements, and it is not clear how the market would respond to publicly announced events of activism. In another study Buchanan and Yang (2007) conduct a comparative analysis of shareholder proposals in the US and UK for the period of 2000-2006. This study does not find any statistically significant results for the UK companies and attribute this to a small size of the UK sample. Again, this paper considers only shareholder proposals without discussing other forms of activism.

McColgan (2001) and Filatotchev et al (2013) argue that a country's legal system is a fundamental determinant of how its governance system evolves. While both the US and UK have the same 'common law' legal tradition, and equity ownership is largely diffused in both countries, the UK investment landscape has a number of legal and institutional differences that may have an impact on the effectiveness of shareholder activism as a governance factor. It can be argued that the UK has more favourable conditions for shareholder activism because of its legal system with fewer limitations on actions of shareholders. For example, the US shareholders cannot call special meetings, unless the company's corporate charter or bylaws allow otherwise. In the UK, shareholders with 10% of voting rights may force the company to hold an Extraordinary General Meeting (EGM). Furthermore, corporate articles of association cannot deprive shareholders of this right (Becht et al., 2009). In the US, shareholders have to carry out a contested solicitation and bear all costs themselves if they want to put forward their board nominees (Cai, Garner, and Walking, 2006). This process usually has low success rates and it is not very popular among investors (Buchanan and Yang, 2007). In contrast, the UK shareholders can replace the board with their own nominees if they managed to win more than half of eligible votes and each director received the majority of votes. Another very significant difference is that in the UK shareholder proposals, once passed, are legally binding, whereas in the US they are non-binding and similar to recommendations. Therefore, rules concerning shareholder meetings, directors' removal and election, and the binding power of shareholder proposals create a more favourable environment for shareholder activism in the UK.

Thus, this paper explores gaps that exist in current research by looking at actual actions of different types of investors and their demands in the UK. Our review of the existing literature suggests mixed evidence with regard to the effectiveness of shareholder activism as a governance mechanism. There is a need to conduct a more fine-grained research in this field. Being a first exploratory study of this nature, this paper does not suggest specific research hypotheses. Instead, we address the following general research questions:

– How does the stock-market respond to shareholder activism events initiated by different types of investors?
– Are there any differences between performance outcomes of different channels of shareholder activism, such as shareholder proposals and public debates?
– Are differences between investor demands associated with different performance outcomes?

Data and Methodology

We collected data on shareholder activism events from 1998 to 2008 by using a number of sources. First, we used Factiva database that provides comprehensive information on corporate events. The primary set of information was collected by searching for all shareholder activism events using combination of words: shareholder(s)/investor(s) activism, activist shareholder(s)/investor(s), shareholder(s)/investor(s) revolt, rebel shareholder(s)/investor(s). In addition, we used a list of registered shareholder proposals from

1998 to 2008 provided by Research, Recommendations and Electronic Voting, a corporate governance advisory service which is part of Risk Metrics Group. This sampling procedure provided information on 270 shareholder activism events targeting 217 firms. In order to be included into our sample, information about an event should have been available to the public through a company's press release or announcement, investor press release or announcement, an interview with the company's or investor's representative, and/or an article in a media source containing description of the event.

Next, we manually collected data on the timeframe of the event, details about investor demands, and types of activism. When a series of events was initiated by the same active investor in relation to the same demand, only the first event was included in our sample provided that the time lag between the first and the second event was less than 6 months. Because of missing data problems, our final sample included information on 101 shareholder activism events. For each company we were able to identify an exact date of the event, shareholder demand(s) and the type of activist investor. There was no significant difference between missing companies and companies included in our sample in terms of size, performance and other firm-level characteristics. Daily share price information surrounding the event was collected for each event using Reuters and Datastream.

In order to analyse the short term and medium term impact of activism on the target firm's value, the event study methodology was used. This approach measures the impact of a specific event on the firms' value using financial market data and examining changes in stock prices around the date of the announcement (MacKinley, 1997). The Market-Adjusted Return Model was used for the calculation of cumulative abnormal returns (CAR), and the FTSE-All Share Index was used for the adjustment.

Results

To evaluate the dynamics of shareholder activism in the UK we started with information on 270 shareholder activism events targeting 217 firms. Various forms of activism were classified into four categories: (a) public debate (e.g., briefings to journalists, press releases, open letters or circulars ahead of general meeting, organising action groups, etc); (b) submitting shareholder proposal(s) to an annual general meeting; (c) calling for and submitting shareholder proposal(s) to an extraordinary general meeting; and (d) litigation actions. Table 1 provides a distribution of shareholder activism events over time and the tactics (forms of activism) that were used by investors. This table shows that in 56% of all cases, shareholders tried to publicly express their concerns rather than directly use their legal rights in order to influence the company's management. This indicates that investors in the UK consider public debate as an effective tool of activism. In 43% of cases investor campaigns resulted in proposals to the company's general meeting. In total, 117 events led to the submission of shareholder proposal(s) and the majority of them were presented at an extraordinary shareholder meeting. In general, the sample reflects an increasing trend in the number of shareholder activism events over time, especially a sharp rise in 2007. Activist investors, as a rule, did not act alone, with 64% of events involving several shareholders acting together and forming pacts with combined voting power. Moreover, institutions in the UK often acted collectively through their professional associations such as the National Association of Pension Funds (NAPF) and the Association of British Insurers (ABI).

- Table 1 near here-

Bearing in mind a diverse nature of activist investors in the UK, they were classified into seven categories: traditional institutional investors, such as pension funds and insurance companies (II), their associations (AI), investment management companies, including asset management companies, investment and unit trusts and funds, investment holding groups (IM), associated companies that have business interests in the target firms (CO), hedge funds (HF), private investors (PI) and other investors such as unions, human-rights groups, and environmental groups.

Our analysis shows that traditional institutional investors and their associations continue to play an important role being responsible for almost one third of the total events. A slight decline of this group's activities in 2005 can be explained by a substantial reallocation of equity ownership in the UK and by an increasing proportion of privately negotiated settlements between organisations and their traditional institutional investors. Other types of investors such as investment managers and hedge funds appear to be increasingly active. In particular, hedge funds initiated a substantial amount of interventions peaking in 2007. There is evidence of a growing number of events initiated by foreign investors, usually the hedge funds. This can be a reflection of a general trend in the ownership structure in the UK that is associated with the growing proportion of equity held by alternative fund managers and investors from the rest of the world, in particular from the US. Private shareholders accounted for 24% of activist campaigns. Within this group, 30% of events were led by former executives (often founders or former CEOs) of the company and private shareholder associations or action groups. Finally, only few activist events were organised or led by social or environmental groups in the UK, possibly because they do not have enough influence and cannot meet high ownership requirements and bear all the costs of activism.

In terms of various types of investor activism, Table 2 shows that traditional investors and their associations seem to rely mostly on different forms of public debates (e.g., press releases, media events, etc). However, this table also shows that hedge funds, investment managers and private investors usually use a variety of tactics in order to achieve their goals. In more than 50% of all cases these types of investors used shareholder proposals put forward at AGMs or EGMs. Private investors are also leading in terms of using legal procedures against the company, but the total number of cases remains relatively small at 2%. It seems that the US-style "litigation culture" is not popular among the UK investors, but there are some signs that legal actions taken by investors may become more popular in the following years.

- Table 2 near here-

All shareholder demands were classified into six broad categories: general governance-related demands (such as board size, proportion of non-executive directors or composition of Board committees); board member-related demands, when investors name specific directors they intend to elect or remove; remuneration demands (e.g., the size of remuneration packages and severance payments of top executives, notice period and other contract terms); demands regarding the firm's capital structure (share buyback, dividend programs and capital restructuring plans); business strategy demands mostly related to corporate divestments, mergers and acquisitions, etc.; and social and environmental demands such as adopting social and environmental standards, workplace policies. Our data shows that board member-related demands appear most frequently (35%), followed by remuneration (22%), business strategy (21%), governance (10%), capital structure (9%) and social and environmental (3%) demands.

The board member or business strategy related demands appear to be the main drivers behind the increase in the number of shareholder activism events. In the US, demands related to the board of directors usually focus on declassifying the board or separating positions of the CEO and Chairman (Buchanan and Yang, 2007). In the UK, 35% of the board-related demands target a replacement of the entire board, or a proxy contest event. A proxy contest is often defined as a process in which outside dissident shareholders mount active solicitations aimed at gaining board control (Gordon and Pound, 1993). Since shareholder proposals in the UK are legally binding, shareholders in the UK have more favourable conditions to nominate and elect directors. Our data suggests that the UK investors use removal or election of a board member or a proxy contest more proactively as an effective mechanism to initiate corporate changes.

A sharp rise of remuneration-related cases in 2003 may be linked to corporate governance debates around a 'reward for failure' and new legislation requiring boards to submit remuneration reports to an AGM. Another type of demands that is used relatively more frequently in the UK is related to business strategy. Investors often target firms' operations or strategic decisions, for example, urging the board to consider selling off company assets or the company itself, opposing an acquisition or a bid from another company. The frequency of this type of interventions has risen significantly in 2007. It seems that worsening economic conditions force investors to intervene with the firm's strategic decisions more often, making firms rethink their business models or future direction in the times of economic downturn. Demands concerning various 'poison pill' mechanisms are mainly absent in the UK, as UK companies do not usually use these anti-takeover defences due to the resistance from institutional shareholders (Black and Coffee, 1994).

Using the event study methodology, we tested the stock-market response to various events of shareholder activism. We started our analysis with looking at the market reaction to the announcements of activism events for the total sample including all types of investors and all forms of activism. Pre-event performance results were negative and statistically significant (p=0.08) which indicates that activist tend to target underperforming companies. Our tests provided some evidence of positive abnormal returns using the short term time frame and negative cumulative returns in the medium term period. However, both results lacked statistical significance indicating that investor activism as a whole has no influence on the target company's market value. A conflicting reaction of the market to the different types of investors and activism events can potentially drive these results, and our subsequent tests explore this issue in detail.

First, we explored the short and medium term effects of shareholder activism events depending on tactics that were used by shareholders. Our sample was divided into two major groups of firms experiencing activism events: public debate and submitting shareholder proposals to the firms' general meeting. Panel A of Table 3 shows statistically significant positive short term effects (3.3% and 3.5% CAR for five days surrounding an event and twenty day period of post-event performance) related to shareholder proposals. These short term abnormal returns reflect an expected value of activism based on market estimation of the likelihood that investor plans will be implemented.

- Table 3 near here-

These results differ from previous research on shareholder activism in the US which failed to find any significant market response. One explanation of this finding is related to a legally binding nature of shareholder proposals in the UK. When a proposal has been accepted by an AGM/EGM, it has to be implemented by the company's management. Figure

1 shows that investors respond positively to this information, and abnormal returns grow steadily after information has been released.

- Figure 1 near here-

Panel B in Table 3 reports the stock price reactions to investors initiating a public debate in order to put pressure on the target company's management. Pre-event negative returns (-2.46%) signal that public campaigns usually targeted at underperforming firms. We did not find statistically significant abnormal return in the short term window after an announcement. However, there is evidence of a negative long-term, post-event performance (-3.7%). This implies that public campaigns initiated by investors do not work effectively to improve company's value. On the contrary, investors seem to consider such news as a sign of shareholders' failure to come to a negotiated agreement with the firm's directors and an indication of deep-rooted problems that may affect performance in the long term.

Second, we looked at stock-market responses to different types of investor demands. Table 4 shows that demands related to the company's directors and business strategy generate positive short term reaction of the firm's share price (4.2% and 5.9% for a five-day event window for board members and strategy demands in Panels A and B respectively). However, there is no significant market response to investor demands associated with executive remuneration (Panel C in Table 4).

- Table 4 near here-

Our findings indicate that the market perceives board changes as an effective tool to facilitate the company's restructuring. Indeed, our data shows that in the majority of cases this type of investor demand involved a nomination of investor representatives on the board. Figure 2 clearly shows that the stock market participants positively respond to board-related demands long after these proposals have been put forward by shareholders. Strategy demands are usually related to business issues where changes could be directly and relatively rapidly reflected in the company's results (for example, a spin-off or divestiture). The medium term results, however, lack statistical significance.

- Figure 2 near here-

Third, we looked at stock-market responses to activist events depending on the type of activist investor. Panel A in Table 5 shows that traditional institutional investors usually target underperforming companies. However, the short term (five days surrounding the event) and medium term (from day three to six month after the event) abnormal returns are negative and statistically significant. Panel B provides similar results for associations of institutional investors. All events in these sub-samples were carried out through public debate, and our result can be a reflection of the market's pessimistic view on such publicity, in line with our findings in Table 3. Moreover, traditional institutional investors rarely publicly put forward demands regarding specific aspects of a company's business or management (such as share buy-backs, spin-offs, or nominations to the board of directors). More often they prefer indirect methods of influence such as face-to-face discussions with the company's management. A combination of this specific form of activism and limited demands seems to lead to a negative stock reaction.

- Table 5 near here-

In contrast to traditional institutions, the hedge fund-initiated campaigns result in a statistically significant positive response (3.0% in a five-day event window, Panel C in Table 5). This reaction can be explained by the specific tactics hedge funds use and their more aggressive demands which fuel the stock market expectations about possible corporate change. This finding is consistent with previous research in the US (Brav et al., 2006). However, as Figure 3 clearly shows, in the medium term the positive abnormal returns appear to be diminishing. It seems that hedge funds in the UK are less successful in achieving their goals and create less value than it was initially expected by the stock market. Also, as it was mentioned before, many of the activist hedge funds are based in US and have great experience in their domestic market, but facing difficulties in realising their strategies in the UK. We did not find any significant effects of shareholder activism initiated by fund managers.

- Figure 3 near here-

Discussion

Our research shows that shareholder activism in the UK is increasing in its economic importance following recent changes in legislation and capital market structure. Taking this into account and bearing in mind substantial resources committed to shareholder activism by corporations and investors, its effectiveness has become an important area for investigation.

Although our analysis did not identify any significant impact of shareholder activism in general on the target firm's performance, a deeper look into the impacts of different types and forms of activism has provided some interesting patterns. Our paper confirms that shareholder activism can create a positive impact; however, its effects on the company's value vary dramatically depending on its form and the nature of investor demands.

Our analysis clearly indicates that the stock market participants take into account a specific form of shareholder activism. The UK legislation improves the effectiveness of shareholder activism in the form of shareholder proposals. In particular, proposals that have been approved by shareholders' vote have a binding power and have to be implemented by management. In addition, the UK shareholders are empowered by their ability to nominate corporate directors and to call an EGM. In the majority of proposals, active investors demanded a replacement of a specific member of the company's board of directors with their nominee or specific changes to the company's business strategy. These demands are seen as more 'aggressive' or 'effective' in terms of facilitating corporate restructuring and change. Therefore, they are likely to have a significant impact on the company's performance, and our analysis confirms these arguments.

In contrast to proposal submission, investor activism in the form of public debate is different in its nature and does not have binding powers or mechanisms to ensure its implementation. As a result, the stock market does not expect this type of change to be implemented or to improve the company's performance. We did not find any statistically significant impact of this form of shareholder activism on the target company's market value in the short and long term, meaning that this form of activism is not the most efficient way of spending resources allocated to shareholder engagement with companies.

Our analysis of the effectiveness of shareholder activism depending on types of demand shows that more aggressive shareholder demands associated with a likelihood of corporate change lead to an increase in the company's value. More specifically, board member- and business strategy-related demands are associated with positive abnormal returns. Demands concerning remuneration issues do not show any significant impact to the firms' market values. Again, these findings call for a more fine-grained research on the economic impact of shareholder activism.

Our evidence also indicates that investors' mechanisms of engagement with companies vary depending on their type, in line with previous research on the governance roles of different types of investors (Hoskisson et al., 2002). This could be explained by the differences in their investment horizons, motivations, strategies and goals that have been identified by previous research. This paper's results show that the stock price reaction to activism may be a complex outcome of a combination of tactics and demands that investors use, rather than their types. For example, our results show that traditional institutional investors (pension funds and investment arms of insurance companies) rarely use options that are provide by the UK law, such as submitting a proposal or calling an EGM. They seem to prefer public debates in order to trigger corporate change. Further, their demands are usually aimed at the firms' governance issues (for example, board independence or size) or remuneration issues. This is a less aggressive way to initiate corporate change and it does not seem to have a direct impact on the company's operations. As a result, this combination of a specific form of shareholder activism and demands has a negative impact on the target company's market value. Compared to traditional investors, hedge funds' activism associated with more direct demands and submission of shareholder proposals leads to a positive market reaction. Our evidence seems to suggest that only shareholder activism in certain forms (shareholder proposal), certain demands (board members and strategy) and by certain types of investors (hedge funds) leads to an increase of the target company's market value.

Previous research related to the effectiveness of shareholder activism has been focused on the US corporate environment, and, in the majority of cases, it failed to find any significant impacts of shareholder activism on the target firm's performance. Our research clearly indicates that corporate governance mechanisms, in particular shareholder activism, do not work in the same way in every country and they may have different levels of efficiency in reducing agency cost depending on the legal and governance environments in a particular country (Filatotchev et al., 2013). The UK experience shows that shareholder activism can be an effective governance mechanism, but its effects are not homogenous and vary dramatically depending on particular combinations of types of investors, their forms of engagement and specific demand. These findings suggest a need to re-think the current theoretical approach to the effectiveness of corporate governance mechanisms.

In terms of practical implications, given the amount of time and resources that are being dedicated to investor activism issues, our findings may be of interest for both investors and the government. Shareholders and companies should develop a more informed approach to shareholder activism in order to avoid value-destroying activities and enhance its positive effects. More specifically, traditional institutional investors and investment managers, while developing their engagement policies, should carefully consider demands and tactics that they are going to use to achieve expected outcomes in order to avoid a decline in the target company's value. More specifically, demands related remuneration or general governance issues should not be combined with public debate tactic but pursued in alternative forms. The periodic reviews and evaluations of the effectiveness of the investors' involvement with the investee firms should be carried out.

This research reveals that the current trends in the UK capital markets, e.g. a relative reduction of equity held by traditional institutional investors and a growing importance of hedge funds and foreign investors, may change patterns of shareholder activism. Hence, its efficiency and impacts on performance may change in the future. Therefore, this research should be updated in order to be able to capture and track these changes.

Limitations

Our study has limitations that may be addressed in future research. First, our analysis is focused on publicly disclosed events of shareholder activism. However, in many cases, shareholders try to negotiate their demands with the target firm's management informally or behind the closed doors. Such activities are not explored in this study, which can lead to an underestimation of the true extent of shareholder activism in the UK. Second, the accuracy of results based on the event study methodology is extremely sensitive to exact dates of events and presence of other information releases surrounding these dates. Thus, the abnormal returns may reflect information other than that related to the event. Another limitation of this study is a difficulty with establishing a causal link between shareholder activism and subsequent medium and long term changes in corporate performance. The observed changes could be a result of public pressure, behind-the-scenes negotiations with activists, or some other influences outside investor activism cases considered in this study. Finally, the effects of dividend payments on share price were not captured in this study. Therefore, it is possible that changes in the firm's value an activist event are underestimated.

Conclusion

This paper gives a detailed analysis of the development of investor activism in the UK during the last ten years by looking at types of active investors, their demands and outcomes of the events. It reveals that shareholder activism phenomenon is becoming more dominant in recent years and that current structural changes in the UK capital market lead to its transformation. The results display noticeable differences in activism by different types of investors, and they call for a more fine-grained and contextualized analysis of this important corporate governance factor.

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Figure 1 Cumulative abnormal returns for shareholder proposals (a 40 days event window).

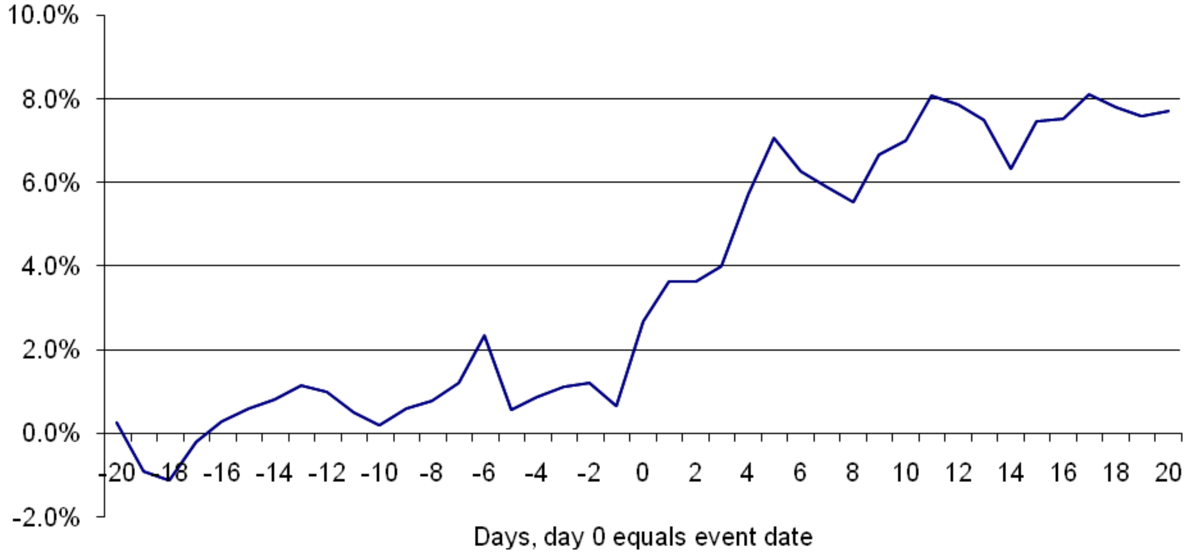

Figure 2 Cumulative abnormal returns for events related to board changes (a 40 days event window).

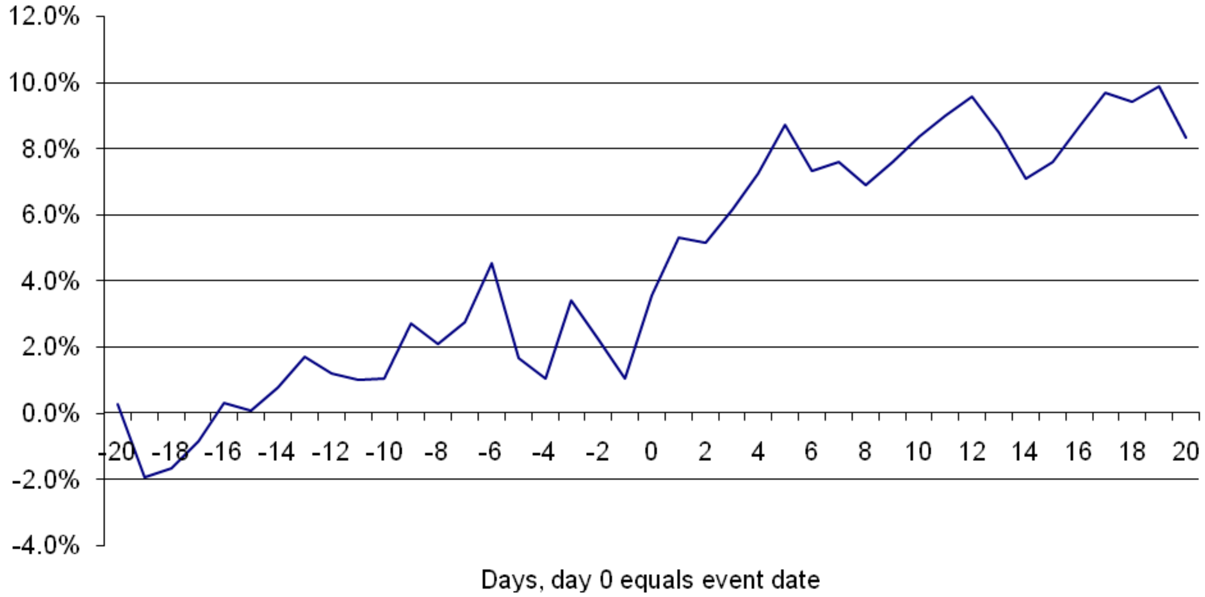

Figure 3 Cumulative abnormal returns for hedge funds' activism events (a 40 days event window).

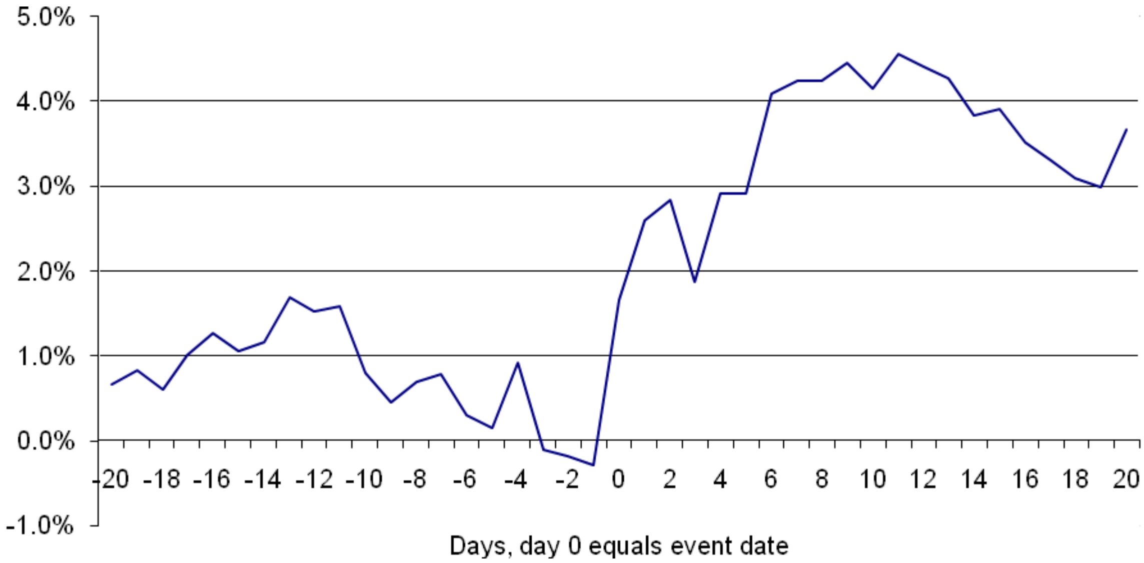

Table 1. Frequency distribution and forms of shareholder activism events in the UK

Form/ Year	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	H1 2008	Grand Total	Overall
Public Debate	5	10	7	8	15	19	16	21	10	26	13	150	**56%**
Proposal, EGM	2	1	8	6	10	6	7	14	10	13	12	89	**33%**
Proposal, AGM	3	1	2	7	2	2	2	-	5	2	2	28	**10%**
Litigation	-	-	-	-	-	1	1	-	-	1	-	3	**1%**
Grand Total	**10**	**12**	**17**	**21**	**27**	**28**	**26**	**35**	**25**	**42**	**27**	**270**	**100%**

Table 2 Shareholder activism events: types of shareholders and forms of activism

Tactic/ Investor	AI	CO	HF	II	IM	Other	PI	Grand Total
Public Debate	100%	57%	39%	98%	46%	13%	37%	**56%**
Proposal, EGM	-	43%	54%	2%	38%	13%	49%	**33%**
Proposal, AGM	-	-	7%	-	14%	75%	13%	**10%**
Litigation	-	-	-	-	1%	-	2%	**1%**
Grand Total	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**

Table 3. Short and medium term cumulative abnormal returns, the two types of activism

Panel A: Shareholder proposals

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	29	0.74%	0.54%	0.326	0.374	51.7%
CAR [-2;+2]	29	3.29%	1.17%	1.602	0.060	67.9%
CAR [+3;+20]	29	3.45%	1.50%	1.801	0.041	58.6%
CAR [+3;+130]	28	0.98%	8.49%	0.157	0.438	57.1%

Panel B: Public debate

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	67	-2.46%	-0.78%	-2.069	0.021	38.8%
CAR [-2;+2]	67	-0.31%	-0.04%	-0.477	0.317	51.6%
CAR [+3;+20]	67	-1.00%	-1.47%	-1.049	0.149	44.8%
CAR [+3;+130]	64	-3.69%	-4.23%	-1.466	0.074	40.6%

Note: The total count of the events in the table does not sum up to 101 because only events with single demand were taken into account.

Table 4 Short and medium term cumulative abnormal returns, different investor demands.

Panel A: Board members related

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	18	1.25%	1.17%	0.491	0.315	55.6%
CAR [-2;+2]	18	4.27%	1.20%	1.638	0.060	70.6%
CAR [+3;+20]	18	0.55%	-1.49%	0.258	0.400	44.4%
CAR [+3;+130]	17	-8.28%	-4.83%	-0.888	0.194	35.3%

Panel B: Business strategy related

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	10	-0.21%	-1.35%	-0.068	0.474	40.0%
CAR [-2;+2]	10	5.94%	2.27%	1.874	0.047	77.8%
CAR [+3;+20]	10	1.56%	2.93%	0.740	0.239	70.0%
CAR [+3;+130]	9	-10.97%	-1.03%	-1.620	0.172	33.3%

Panel C: Remuneration related

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	35	-0.78%	-0.28%	-0.551	0.293	45.7%
CAR [-2;+2]	35	0.10%	-0.04%	0.137	0.446	50.0%
CAR [+3;+20]	35	0.47%	-0.64%	0.371	0.356	48.6%
CAR [+3;+130]	34	-2.95%	-6.22%	-0.836	0.205	35.3%

Note: The total count of the events in the table does not sum up to 101 because only events with single demand were taken into account.

Table 5 Short and medium term cumulative abnormal returns, different types of investors

Panel A: Traditional institutional investors

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	25	-2.39%	-0.28%	-1.475	0.077	48.0%
CAR [-2;+2]	25	-2.01%	-0.27%	-1.883	0.036	36.0%
CAR [+3;+20]	25	-0.94%	-1.52%	-0.572	0.286	36.0%
CAR [+3;+130]	25	-8.08%	-8.59%	-2.685	0.006	24.0%

Panel B: Associations of institutional investors

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	12	-2.25%	-1.88%	-1.293	0.111	33.3%
CAR [-2;+2]	12	0.93%	1.40%	1.001	0.169	58.3%
CAR [+3;+20]	12	-0.12%	-2.70%	-0.061	0.476	41.7%
CAR [+3;+130]	11	0.50%	3.33%	0.105	0.459	54.5%

Panel C: Hedge funds

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	17	-1.03%	-1.73%	-0.435	0.335	35.3%
CAR [-2;+2]	17	3.10%	0.30%	1.555	0.070	58.8%
CAR [+3;+20]	17	0.48%	1.50%	0.260	0.399	52.9%
CAR [+3;+130]	16	-4.84%	-0.55%	-0.857	0.202	43.8%

Panel D: Investment managers

Event window [days]	N	Mean	Median	t stat	p value	% positive
CAR [-10;-3]	21	-4.67%	-3.01%	-1.544	0.069	42.9%
CAR [-2;+2]	21	0.55%	1.26%	0.374	0.356	66.7%
CAR [+3;+20]	21	-0.63%	0.45%	-0.250	0.403	52.4%
CAR [+3;+130]	19	3.88%	5.89%	0.524	0.303	57.9%

Note: The total count of the events in the table does not sum up to 101 because only events with single demand were taken into account.