Activist Investing in Europe

2021

Activistmonitor
An Acuris company

Skadden

Contents

Foreword

Activist pressure set to swell in post-Covid Europe

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As the Covid-19 crisis continues to create uncertainty for companies' long-term plans, everything points to increased shareholder activism in Europe in 2021 and high pressure on issuers in the near future.

No European issuer should consider itself immune from an activist attack. As illustrated in the past, activists do not limit their demands and campaigns to one or few sectors in particular. On the contrary, and despite the fact that financial institutions and certain industrials have recently been in the spotlight, all sectors are concerned.

Size does not change a thing. Small, mid or large capitalisations will not divert activists from a potential opportunity. Recently, activists have demonstrated their ease in finding new allies among private equity funds or institutional investors, allowing them to focus even more easily than before on the largest issuers.

Whatever the sector, whatever the size, activists will focus on issuers with potential vulnerabilities, sometimes assuming that the larger the prey is, the larger the financial reward may be. Companies whose share price has not recovered to pre-pandemic levels may be particularly vulnerable.

Activists have understood that, for public campaigns, it is beneficial to appear as champions of noble and challenging causes, such as ESG, in order to be taken more seriously or to increase the likelihood of being supported by other investors. ESG and corporate social responsibility must be taken into account more and more by issuers, at a minimum to face potential activists' complaints.

For those issuers who have not been able to benefit from the 2020 interlude to conduct an in-depth analysis of their strengths and vulnerabilities with respect to shareholder activism, they will have to anticipate demands, and quickly prepare themselves for any potential action from activists.

No European issuer should consider itself immune from an activist attack.

Activists ready to do battle

2021, a year replete with potential flashpoints, will see a surge in shareholder activism. European companies must steel themselves for the challenge.

Europe's activist investment arena is becoming more and more crowded, with increasingly savvy homegrown activists and their international counterparts targeting companies across the region. Newcomers are rubbing shoulders with established players, and smaller outfits are proving their size is not a barrier to success.

This report, with the help of statistics from Activistmonitor, examines the state of shareholder activism in Europe. With new data gleaned from anonymised interviews with corporates and activists alike, it presents a vision of how the space is likely to develop in 2021 and beyond.

The Covid-19 pandemic might have been expected to stifle activism over the past year, but this is not what transpired; instead, activists refused to back down from existing confrontations and continued to launch campaigns. Many also sprang at opportunities to build their stakes in target companies.

There is hardly a reason to expect this trend to reverse: corporates and activists alike expect activity levels to remain elevated in the near term. With huge pressure on boards to articulate a compelling vision of how they will build back better from the crisis, flashpoints are inevitable. The additional impetus given by the pandemic to environmental, social and governance (ESG) concerns provides a further source of potential confrontation.

Activists are ready for the fight. They have a clear view of where they will engage and the demands they will make. Corporates must be equally prepared. Boards' best chance of avoiding a disruptive and damaging public confrontation with activists lies in heading off such campaigns in the first place. But that cannot be left to chance.

In this context, this report provides key insights into how shareholder activism in Europe will develop over the year ahead – and how corporates should ready themselves accordingly.

Our key findings include:

80%

1. The vast majority (80%) of corporates surveyed anticipate an **increase in shareholder activism post-pandemic**, including 54% who expect a significant increase.

2. Most activists surveyed (60%) expect **overall campaign volumes to return to their pre-pandemic levels** before end-2021.

3. Companies in Europe should, over the next 12 months, be most mindful of **becoming targets from North American activists**. All activists surveyed agree that companies should be very concerned about that possibility, as do 97% of corporate respondents.

60%

4. 60% of corporates consider that 'over the next 12 months, activists in Europe will increasingly employ a strategy of **visible, public activism**, as opposed to one of private, 'quiet', confidential activism'. However, among activists surveyed, four-fifths disagree with that statement.

5. Corporates remain sceptical with respect to activists 'prioritising ESG issues in their campaign demands' – 37% are ambivalent, and a further 35% either disagree or strongly disagree. But activists are firmly in the affirmative: all activists surveyed agree with that statement, including 67% who strongly agree.

6. To mitigate the chances of campaigns arising, most activists surveyed **consider maintaining transparent disclosure practices and promoting broader shareholder engagement** as by far the most important measures that companies should take.

89%

7. Most corporate respondents would support (89%, including 60% who strongly agree) the **evolution of the legal framework** with respect to activist investors and public campaigns over the next 12 months. A sizeable minority of activists (27%) also agree with the idea.

Methodology

In late Q4 2020 and early Q1 2021, Acuris Studios surveyed 35 corporate executives from listed companies and 15 activist investors from the UK, France, Germany, Italy and Switzerland to gain insights into key trends in Europe's activist investing space. All responses are anonymous and results are presented in aggregate.

Covid crisis rewards proactive firms

The pandemic deterred activists only briefly. Vigilant and communicative boards were best placed to withstand 2020's ordeals.

Amid the unprecedented turmoil of the Covid-19 pandemic, shareholder activism spiked over the past 12 months. With markets in turmoil and businesses in many sectors plunging into uncertainty, boards faced demanding questions from investors both behind the scenes and, albeit to a lesser extent, in public confrontations.

"The first half of the year was slower because activists had to focus on their own issues and get familiar with the 'new chess board'," reflects Armand Grumberg, head of Skadden's European M&A. "But in the second half, activism surged for two reasons: first, some campaigns had been deferred because of the initial stages of Covid-19; and second, new investment opportunities resulted from the pandemic itself."

The survey conducted for this report underlines this point: just 3% of companies surveyed said their board had received no approach at all (either privately or publicly) from activists since the onset of the pandemic. Almost two-thirds (63%) said they had been approached once or twice, with a further 34% revealing they had received three or more such approaches.

Data from Activistmonitor reveals the scale of the increase. By end-2020, the total number of live campaigns in Europe had reached 279, a year-on-year increase of 12.5%. That included 60 new campaigns launched by activists, of which 53 were new live campaigns (where the activist had both disclosed a stake in the business targeted and issued at least one public demand). The remainder were potential campaigns, with activist interest reported or disclosed, but public demands not made or not yet made.

This latter category, in addition to the constellation of confidential discussions between companies and activists, cannot not be overlooked, says Holger Hofmeister, a partner in Skadden's Frankfurt office. "This behind-the-curtain activity was significantly elevated. It is behaviour that corporates must still address," he says.

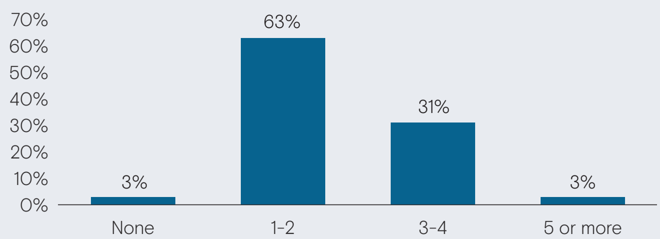
Activists seize on pandemic unrest

Activity was spread throughout Europe. Activistmonitor recorded increases in year-on-year activity in Germany (where there were 10 new live campaigns launched in 2020), France (seven), the Netherlands (six), Italy (four) and Belgium (three).

As in previous years, shareholder activism was most prevalent in the UK, though the 15 new live campaigns launched there in 2020 marked a decline from 2019's total of 22. Activity also fell in Switzerland, where activists launched only three new live campaigns, down from 10 in 2019.

In addition to activism's broad geographical reach, last year also saw companies of every size targeted. Smaller businesses did see slightly fewer activists compared to 2019, but there were still 24 new campaigns launched against companies with a market capitalisation of less

Since the onset of the pandemic, how often has your board been approached (privately or publicly) by activists?



Total Campaigns by Market Capitalisation (Live & Potential)

Market cap	2019	2020	Growth
<USD 1bn	26	24	-8%
USD 1-2bn	12	7	-42%
>USD 2bn	24	29	20.83%
Total	**62**	**60**	**-3.23%**

than US$1bn (down from 26 the year prior), and seven new campaigns at those worth between US$1bn-US$2bn (down from 12). Among larger businesses with a market capitalisation above US$2bn, the number of new campaigns rose from 24 in 2019 to 29 last year.

What is propelling this activity? Our research suggests a correlation with the outbreak of the Covid-19 crisis, with shareholders in companies across Europe anxious for reassurance about the potential effects of the pandemic. As the CEO of one UK corporate put it: "Demand for our services was lower due to the pandemic, resulting in loss of revenue. Discussions with shareholders helped us draw up a clear road map that was acceptable to all parties."

Matthias Horbach, head of Skadden's German M&A practice, underscores the outsized impact of the crisis. "Activists and corporates suddenly had to reassess their view of the business," he says. "The pandemic was a new situation for everyone, and it took time to assess, but we saw the response come through in the third and fourth quarters."

Activistmonitor's data reinforces this message, with businesses in an array of sectors facing challenges from activists. Eight new campaigns were launched that involved the consumer and leisure sector, which faced some of the most arduous disruption in 2020. Financial services – the busiest sector for activists, logging 15 live campaign launches – has also faced significant headwinds, with banks, insurers and others hit with rising bad debts and expensive claims. Industrials (with 10 new campaigns), for their part, had to contend with a collapse in demand and supply-chain turmoil.

Soothing anxious shareholders

The impact of the pandemic is evinced, too, by the types of demands made by activists in 2020. Most strikingly, the number of demands related to cost reductions or

Live campaigns in Europe

operational improvements quadrupled from four in 2019 to 16. Clearly, shareholders had material concerns about the effect of Covid-19 on the bottom line.

There was also a significant increase in demands for discussions with companies – seven in 2020, up from only one the prior year – reflecting the broad-based anxiety that many investors have about the damage wreaked by the pandemic. It is also notable that, in a year when many companies felt compelled to slash dividends, there were 11 demands made in open live campaigns for share buy-backs, dividend increases or returns of capital.

Still, the most common demands made by activist investors in 2020, just as in the year before, involved board and management changes. These accounted for 42 of the 142 demands that shareholders made in 2020. In other words, many activists continue to pursue fundamental, high-level change through their campaigns.

Similarly, M&A continued to be a significant point of concern, with activists making 28 demands for either bolt-on, divestiture or spin-off deals (15) or for the presentation of strategic alternatives, including mergers (13). Inversely, there were also 11 demands opposing boards' M&A proposals. Following the pandemic-induced dealmaking freeze in Q2 2020, activists were evidently keen to make their voices heard during the H2 thaw.

Staying ahead of the curve

Of course, not all shareholder activism last year was related directly to Covid-19. Even in the consumer and leisure sector, for example, there were key campaigns that pre-dated the pandemic, such as Bluebell's demands of Hugo Boss, which contributed to the decision by the company's CEO to step down. In the technology sector, two of the four live campaigns launched last year related to Wirecard's collapse.

Nevertheless, the seismic impact of the pandemic on activism is clear, with many boards anxious about the increased potential for confrontation with shareholders. Almost three-quarters of corporates (74%) surveyed for our research say their boards have proactively discussed the threat of activist campaigns more often than usual since the onset of the pandemic. That includes 43% who say such discussions have occurred far more than usual.

Evidently, boards are working hard to stay ahead of the curve. Almost every corporate surveyed (97%) said that they had, as a result of the pandemic, identified new weaknesses that activist investors might seek to raise. Of those, 60% have already held discussions with shareholders about those issues.

"Amid the pandemic, we identified weaknesses related to our supply chain," says the CEO of one Swiss company. "Discussions with shareholders took place a while ago to reassure them of our efforts to get inventory and procurement activities back on track."

Demands made in open live campaigns

	2018	2019	2020	Y-o-Y 2020
Discussions	1	1	7	600%
Oppose bolt-on/ Divestiture/Spin-off	3	2	1	-50%
Special meeting	1	2	0	-100%
Cost reductions/ Operational improvements	8	4	16	300%
Share buy-back/Dividend/ Return of capital	11	10	11	10%
Bolt-on/Divestiture/ Spin-off	24	16	15	-6.25%
Oppose acquisition/ Merger agreement	2	10	10	0%
Strategic alternatives incl. merger	21	15	13	-13%
Capital allocation/Structure changes	8	7	10	43%
Governance changes	22	18	16	-11%
Board and Management	58	35	42	20%
Environmental/Social changes	0	0	1	NA
Investment disclosure/ update	0	0	0	NA
Total	**159**	**120**	**142**	**18.33%**

As a result of the pandemic, have you identified any new weaknesses that could be raised by activists in potential campaigns?

An Italian corporate CEO says businesses have a window of opportunity to forestall activists. “We want to see if we can manage these weaknesses before any of them are highlighted by activists in potential campaigns,” he explains. “Activists have been somewhat reluctant to hold campaigns because of the Covid-19 crisis.”

Other companies are confronting the threat of an increase in activism in different ways. In the wake of the crisis, more than a quarter (26%) of corporates surveyed say they will be adopting ‘poison-pill’-type provisions, and a further 37% say they had considered it. However, a sizeable share (34%) say they had not considered the possibility at all at the time of our survey.

Europe’s most active activists
Switzerland-based Teleios Capital Partners was last year’s busiest activist investor in Europe. It launched six new public campaigns and issued demands to Maison du Monde, Card Factory and Quadient.

> US funds have been watching and waiting… I think it’s reasonable to expect them to come back to Europe.
>
> Scott Hopkins, Skadden

In second place was Bluebell Capital Partners, one of the six UK-based activists in the top 10. It launched four new campaigns, though two of these – Hugo Boss and Lufthansa – were resolved within the year.

Only one US activist features in the top-10 list, namely Elliott Management. The firm launched campaigns against NN Group and Sampo, as well as Arkema, where it has not formally demanded changes but has seen the company announce several divestments. Scott Hopkins, who leads Skadden’s UK public M&A practice, anticipates a resurgence in US activists in the year ahead. “The US funds have got huge amounts of dry powder and they’ve been watching and waiting,” he says. “I think the reasonable expectation is that they will be coming back to Europe.”

Corporates 'need to be their own activist'

For companies facing activists from Europe and abroad, forewarned is forearmed. More broadly, more confident shareholder engagement will be indispensable.

The pandemic will continue to influence investor activism in 2021 and beyond, with the effects of the crisis likely to be felt by businesses for years to come. Equally, as the crisis recedes – with vaccines beginning to make an impact, at least in advanced economies – other issues will return to the fore.

1 Activists expected to raise their voice

The corporates surveyed for this research expect the uptick in activism noticed in H2 2020 to continue, and even to accelerate. As the fallout from the pandemic becomes clearer – and as government stimulus perhaps begins to wane – 80% predict an increase in activism levels, including 54% anticipating a significant increase. By contrast, fewer than one-in-10 (9%) predict even a moderate decrease.

Activists themselves seem to share this outlook. More than half (53%) expect to be involved in at least three or four campaigns over the next 12 months, while a further third (33%) anticipate five or more confrontations. Most (60%) also forecast overall campaign volumes returning to their pre-pandemic levels before end-2021, and none expects to have to wait until after 2022 for that to be the case.

This is unsurprising, says the head of business development at one French activist. "Considering the impact of Covid-19 on European markets, activists from the region and the US will be interested in accelerating companies' growth objectives," the executive says. "Boards are relying on organic options and slacking on key growth objectives – activist investors have to raise their voices."

Businesses significantly hit by the pandemic will be expected to set out credible recovery plans – and new plans will assuredly attract new challenges. The reshaping of many markets in the wake of the crisis will precipitate demands for corporates to adjust their portfolios. Economic dislocation caused by the pandemic will give rise to opportunistic moves by stronger businesses.

> Considering Covid-19's impact on Europe, activists from the region and the US will be interested in accelerating companies' growth objectives.
>
> Head of Business Development of a French Activist Investor

"We strongly believe there will be a surge in activism – you're going to have a very explosive mix," say Skadden M&A partners Armand Grumberg and Arash Attar-Rezvani. "There will be a number of companies that haven't yet recovered from the impact of Covid-19 and are therefore more vulnerable. Plus, activists are now familiar with the new Covid-19 chess board. Then you have the additional interplay of traditional activists partnering up with institutional investors or private equity houses, which should lead to an increase of activism."

One striking finding in this research is that many corporates are expecting to see hostile takeovers become more common post-crisis. Almost three-quarters (74%) predict an increase, including 48% anticipating a significant increase. Boards presiding over weakened companies will need to be on the lookout for unsolicited offers, with opportunists set to pounce.

Living in 'the new normal'

It may be the boards of UK companies that have most to worry about. Almost half (47%) of the activists surveyed cite the UK as the number-one market in Europe for campaign opportunities in the next 12 months. Germany, for its part, attracts 20% of activists' first-place votes, plus a further 40% of second-place ballots. France and Italy also garner much consideration, while, strikingly, no activists tip Switzerland as a venue for notable opportunities in 2021.

The profound impact of the pandemic on the UK economy is undoubtedly part of this story – the country suffered a sharper slowdown last year than any other G7 nation, according to International Monetary Fund estimates. But the uncertainties of Brexit have added to the turmoil facing British companies.

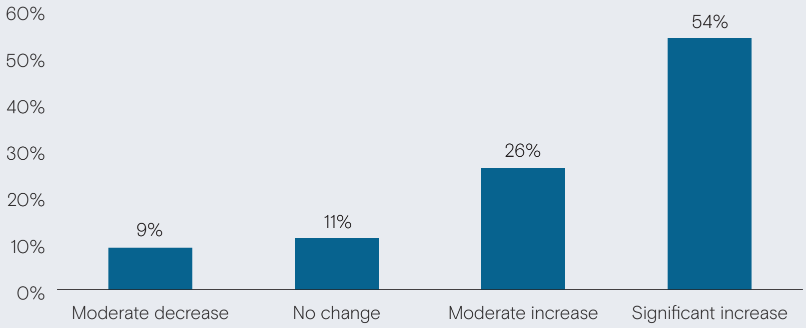
"I expect the UK to offer the most opportunities," says a partner in one UK-based activist investor. "There have been several disruptions over the past months, first due to Brexit and then the spread of coronavirus; investor activism will increase at a faster pace."

As for Germany and France, the CEO of a French activist points to the freedom that such investors have to operate in these markets. "There are fewer constraints on campaigns in France and Germany," they explain. "Some were delayed due to the Covid-19 crisis, but I think those will resume now that people have accepted 'the new normal'."

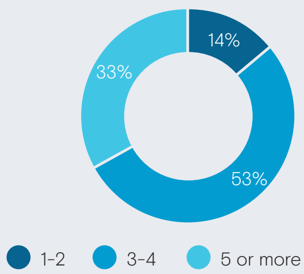
US activists eyeing up European opportunities

Aside from domestic activists, survey respondents expect to see their US counterparts return to

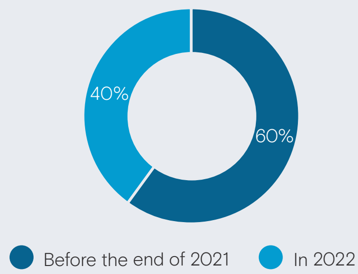
What type of evolution in activity are you anticipating in shareholder activism post-pandemic?



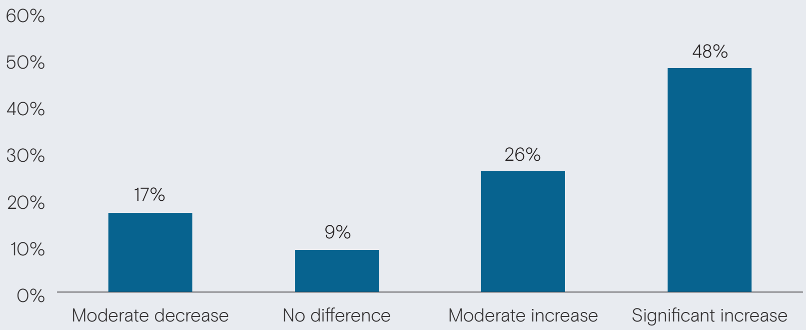
How many activist campaigns do you expect your organisation to be involved in over the next 12 months?



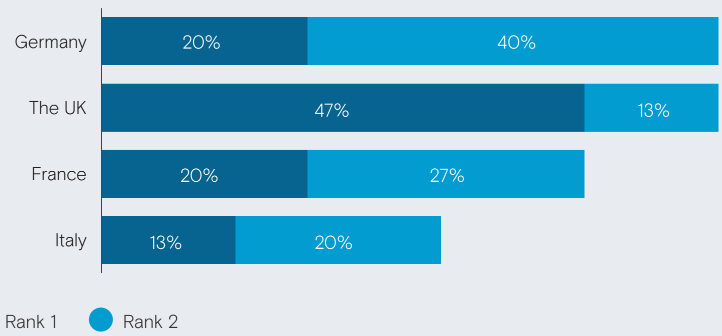
Given the impact of COVID-19 on the global economy, when do you expect overall activist campaign volumes to return to their pre-pandemic levels?



How will the volume of hostile takeovers in Europe change post-pandemic?



Which European markets do you expect to offer the best opportunities for activist campaigns over the next 12 months? (Select top two and rank 1–2)



the fray in Europe. While only one US activist (Elliott Management) featured in the top 10 of most activist investors in Europe last year, almost every survey respondent warns that boards should be very concerned about being targeted by North American activists in 2021. UK activists are also set to play a significant role – more than 70% of respondents suggest boards should be very concerned. As for those from mainland Europe, 60% of activist investors and 49% of corporates, respectively, make the same warning.

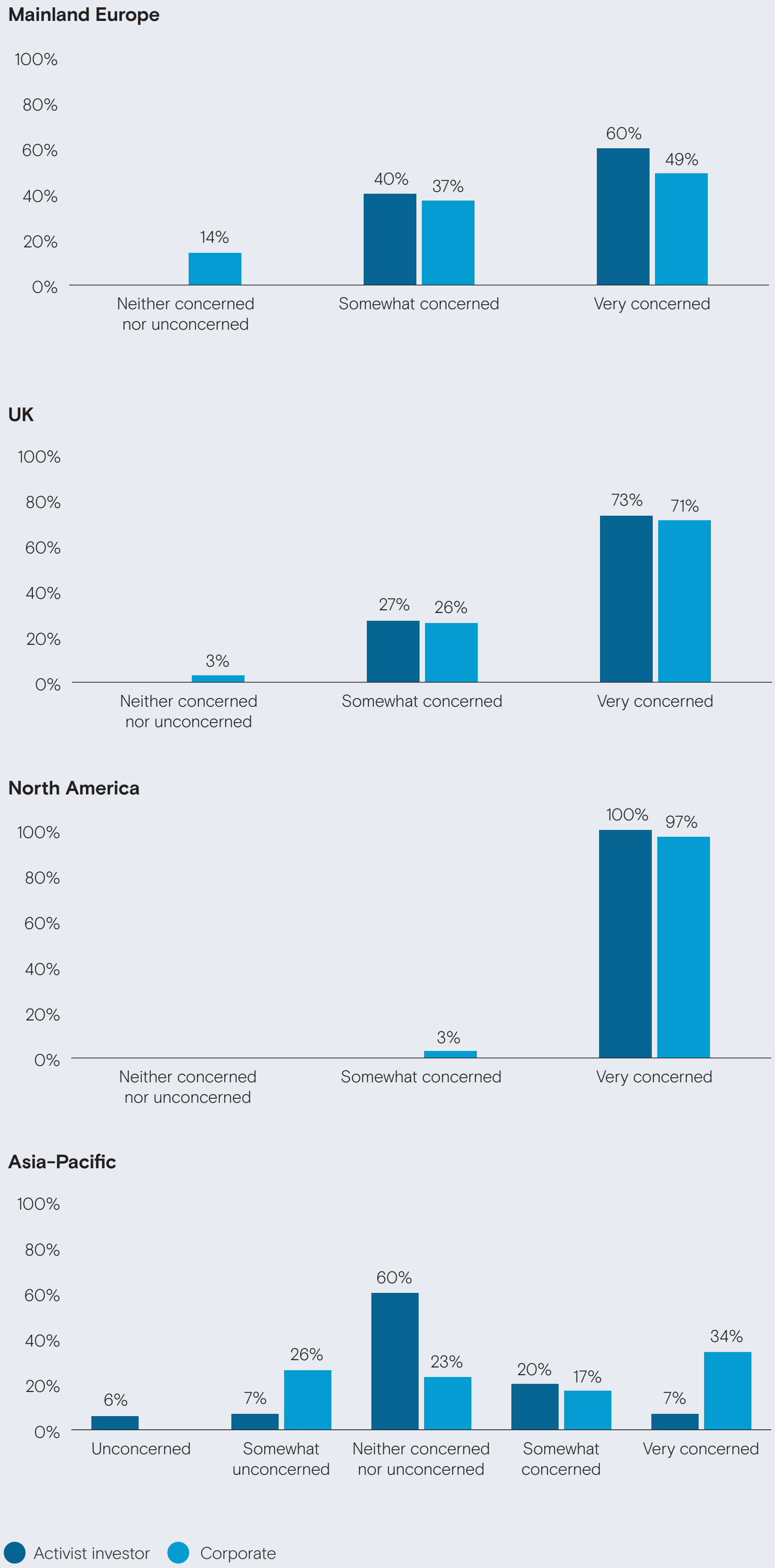
"North American activists have started to target niche European markets, owing to a need to diversify and invest in companies abroad," says the CEO of a French corporate. "The US is bogged down by regulatory hindrances and geopolitical tensions, so activists there will want to see faster results from their European investments," adds a partner in a UK-based activist investor.

"We are going to see a mix," predicts Mariel Hoch, partner in the corporate team at Zürich-based Bär & Karrer. "We have the large international activists, including the North American funds, that can target even the biggest companies. Then there are the regional and country-based activists that may target the smaller businesses."

Some sectors will attract more attention than others. The activists we surveyed pick out technology, media and telecoms (attracting 27% of first-place votes), financial services (also 27%) and consumer and retail (20%) as the industries where campaigns will be most elevated in 2021. Corporates largely agree on TMT (26%) and financial services (17%), but also view industrials & chemicals (20%) and energy, mining & utilities (14%) companies as likely targets.

One key concern for boards is how activists will pursue their objectives. This research may offer some comfort: while 74% of corporates worry that activists are set to step up their public campaigning, rather than more private, 'quiet' engagement, 80% of activists disagree with this

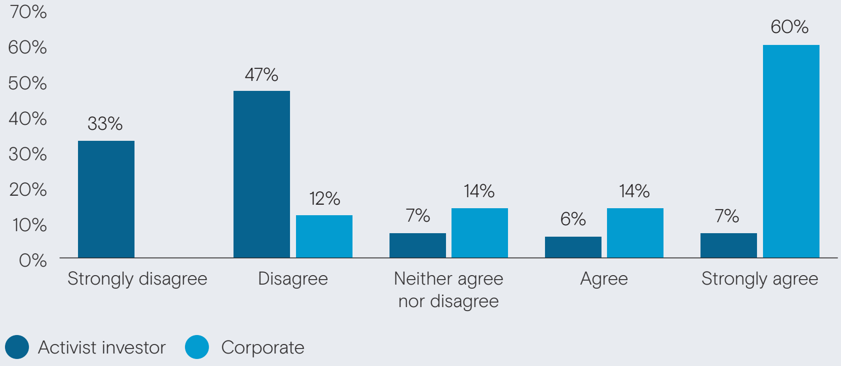
To what extent should companies in Europe be concerned about becoming targets from activists based in the following regions over the next 12 months?



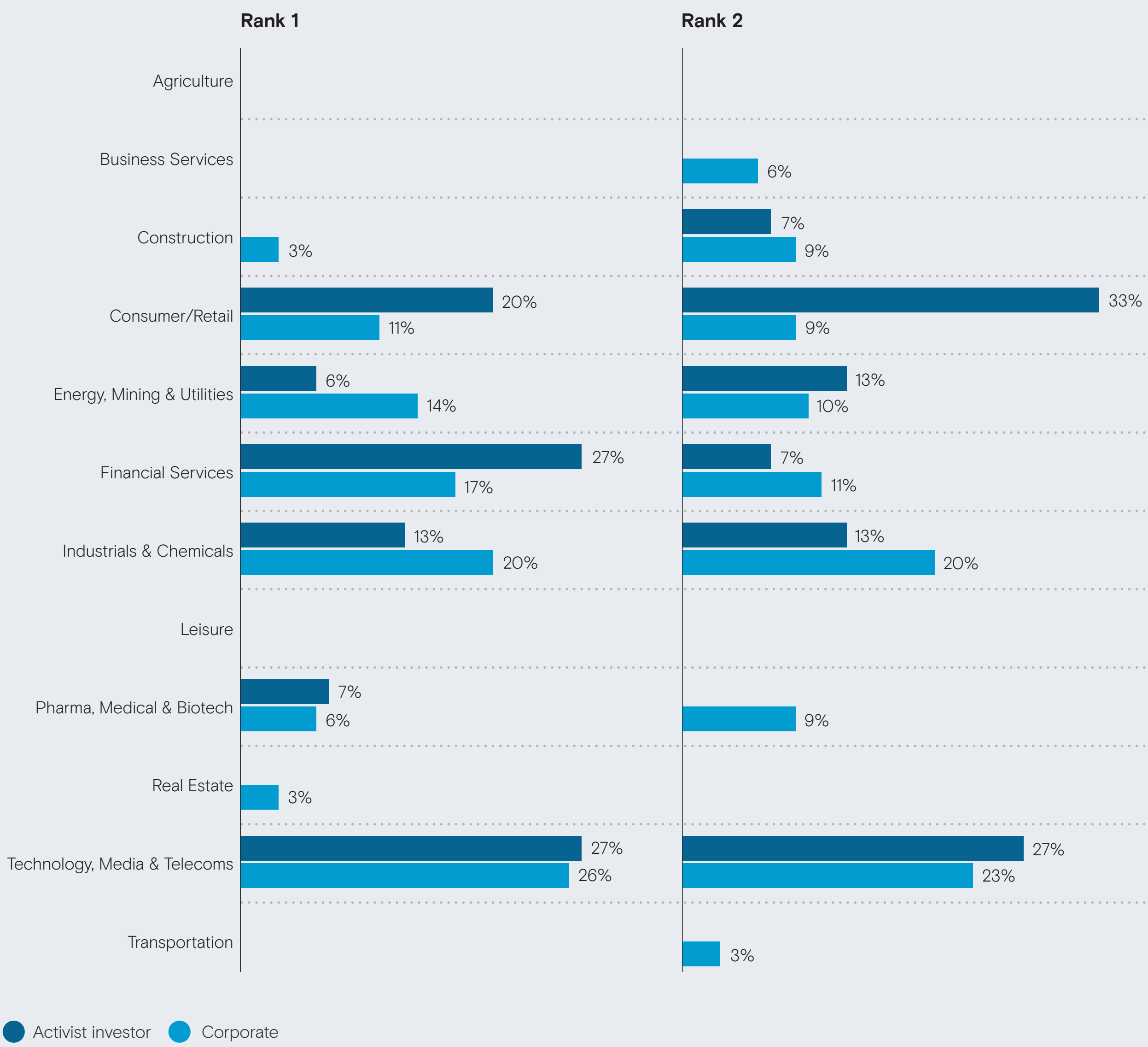
suggestion, including 33% who strongly disagree.

"Activists don't want to affect the company negatively, as falling share prices will cause their dividend to decrease," says the CIO of a UK-based activist investor. "The next 12 months will be crucial for gaining strength in the market. With a public activism strategy, a company's operations could be unnecessarily disturbed," agrees the managing director of an Italian investor. "Activists will wait for a better opportunity."

Do you agree with the following statement: 'Over the next 12 months, activists in Europe will increasingly employ a strategy of visible, public activism (i.e. public letters, media & campaigns), as opposed to one of private, 'quiet', confidential activism.'?



In Europe, in which industries do you expect to see the most activist campaigns over the next 12 months? (Select top two and rank 1–2)



2 What activists want

Activists have clear objectives in mind as they look to a year of heightened activity. Almost half (47% of first-choice votes) of those we surveyed say the demand they expect to make most often over the next 12 months is for changes to the board. A third (33% of second-choice ballots) place share buy-backs and dividends-related demands second on their list of priorities.

For boards, it is important to recognise that their perceptions of activists' motivations may be off the mark. More than a third (34%) of corporates surveyed believe that activists that demand board change are primarily concerned about board tenure, while 26% think lack of specific expertise is what investors are worried about. By contrast, activists themselves overwhelmingly point to lack of independence as the most likely driver of a campaign for changes to the board, with 79% citing this factor. Almost half of activists surveyed (47% of second-choices votes) say concerns about shareholder returns also underpin such campaigns.

Both these issues have been thrown into sharp relief by the pandemic. Activists worry that boards may become overly entrenched, lacking the vision to move companies beyond the crisis – and, as a result, that shareholder returns will not reach pre-pandemic levels.

Fear of dilution is one factor, argues Andrea Sacco Ginevri, partner at Chiomenti in Rome. "One reason to expect an increase in shareholder activism is that so many public companies are in urgent need of recapitalisation," he says. "Shareholders worry about losing power and activists are interested in getting qualified holdings."

Some corporates understand the circumstances better than others. "Activist investors will focus on changes to the board and governance changes," predicts the CEO of one Swiss company. "They believe these are the main reasons for potential failure, so post-pandemic especially, they will demand new personnel and changes to management."

Balancing rebuilding with innovation

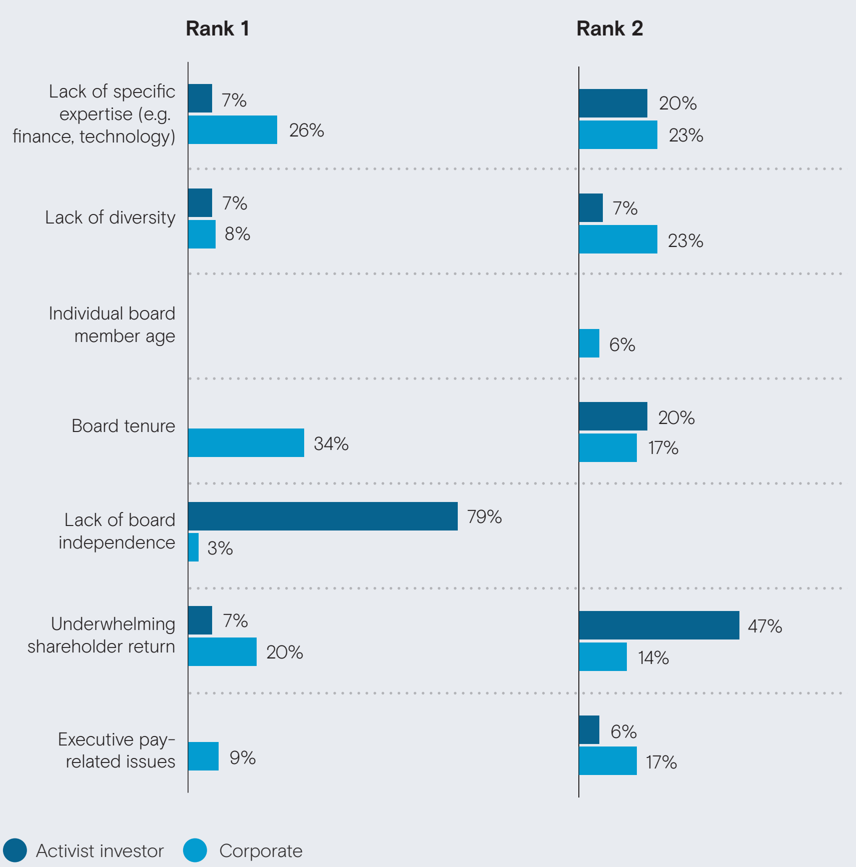
On share buy-backs, dividends and returns of capital, activists have inevitably zeroed in on the pandemic's effects on distributions to shareholders last year. The value of dividends in many countries plunged last year, as boards faced a cash crunch – total pay-outs in the UK, for example, fell 44% – and there are widespread concerns that any recovery in 2021 will be muted, or perhaps even heavily undermined by troubles with vaccine distribution or the spread of coronavirus mutations.

Against this backdrop, all shareholders are looking for comfort, and activists are set to push the issue hard with boards. "Activists are becoming more assertive about dividend issues," says the managing director of one Italian activist investor. "In the past, buy-backs would not be discussed publicly, but conditions have changed quite a bit in light of current circumstances."

Corporates, too, recognise the direction of travel, even if they are unsure how exactly to respond. "Public companies are facing difficult choices, because most of their short-term plans will have been affected by Covid-19," says the CEO of a Swiss corporate. "Activists will pursue dividend issues more strongly because of the unstable investment and trading conditions."

The question will be whether the performance and balance sheet strength of corporates in 2021 gives them room to manoeuvre. Every corporate surveyed for this research believes share buy-back and dividend issues will be an area of particular focus for activists in

What are activists' main motivations when demanding changes to the board/ management of a company? (Select top two and rank 1-2)



the year ahead (with 80% of activists in agreeance). But companies' ability to increase dividends or contemplate returns of capital will obviously depend on their trading prospects and broader market conditions.

This gives rise to a profusion of potential flashpoints, with boards arguing that their hands are tied and activists pointing to areas of the business where they see room for improvement. "With underperforming units, usual dividend fulfilment can't be expected. 2021 will be tough on a few industries trying to regroup," warns the CEO of a Swiss corporate. On the other hand, the head of business development at a French activist investor complains: "Companies have not been innovative in terms of operational improvements; they could be more focused."

3 How boards must respond

Corporates should brace themselves for the anticipated surge in activism in 2021. The priority must be to head off campaigns long before they have even the chance to devolve into public confrontations. But that will not work in all cases – some boards will inevitably need to think hard about the defensive tactics required in such hostile situations.

"You need to be your own activist," suggests Skadden's Scott Hopkins. "Take a hard look at yourself in the same way an activist would in order to identify weaknesses. It's a good thing to do just as a matter of proper governance. Often, companies that do this exercise actually perform better, regardless of whether an activist ever pitches up."

It is worth bearing in mind that a public campaign is often the last thing activists want, adds Skadden's Holger Hofmeister. "It's pretty burdensome and the outcome is pretty unclear," he points out. "The discussion can get out of control, politicians may get involved, and it may become really messy."

Still, our research suggests many boards may need to do more work to avoid public campaigns. Corporates' outlook on how to appease activists clashes somewhat with the views of activists themselves.

Asked which preventative measures are likely to prove most effective in mitigating the chances of activist campaigns arising, 26% of corporates say it is important to engage frequently with a regular set of advisers who can provide an accurate picture of investors' concerns. A further 26% focus on the need to maintain transparent disclosure practices with shareholders, while 17% point to the need for broader engagement with investors.

By contrast, activists are almost twice as likely to focus on disclosure practices, which 47% say can help head off campaigns, while 33% cite broader shareholder engagement. They are far less likely to be impressed by the idea of advisory groups – perhaps fearing these will stand between them and the board – with only 7% of activists citing these as an effective mitigation measure.

The rise of ESG

For many people, an enduring impact of the pandemic is heightened awareness of social inequity and economies' dependence on fragile, global supply chains. This has the potential to spur even more rapid development of the ESG movement, forcing boards to think hard about issues such as climate change mitigation and encouraging activists to move such matters up the agenda.

"Activism and stewardship are blurring closer, and we do now see some activists with a reputation taking this angle," says Bruce Embley, a partner in Skadden's London office. "Bear in mind, too, that the governance component of ESG has always been a fundamental piece of the activist toolbox."

Activists already seem more ESG-minded than boards realise. In this research, while just 28% of corporates agreed with the suggestion that activists will increasingly prioritise ESG issues in their campaign demands, every single activist surveyed did accede to this view, including 67% who agreed strongly.

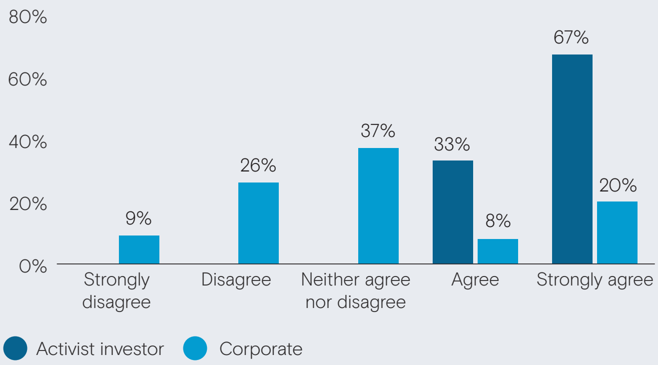
This is not just a Covid-19 phenomenon, but rather part of an ongoing trend. In recent history, activists made it very clear they intended to push corporates to adhere to the guidelines issued by the Sustainability Accounting Standards Board and Task Force on Climate-related Financial Disclosures.

As the policy agenda continues to evolve, so too will the positions taken by activists, suggests Giovanni Filippo Pezzulo, managing counsel at Chiomenti in Milan. "The mix of legislation at one end and the growth of ESG-related funds at the other means European and US activists will target these issues in 2021," he says.

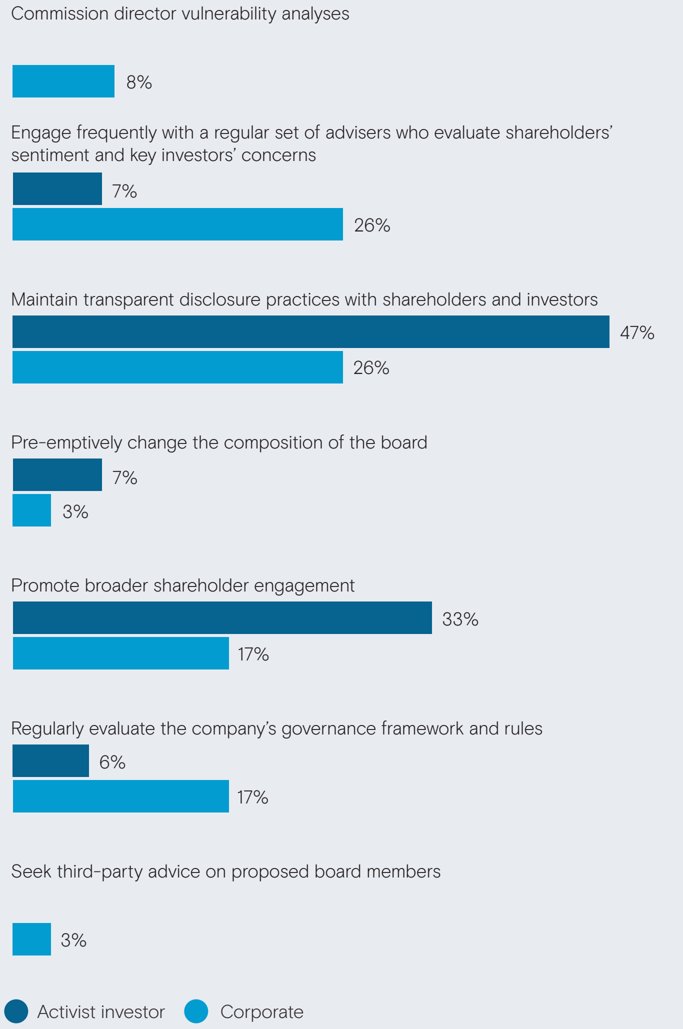
Some activists believe corporates still are not taking ESG matters sufficiently seriously. "ESG issues will feature in many campaign demands because companies don't follow through on their ESG commitments," says a partner of one UK-based activist. "They just touch on and brush over the major issues to protect their image."

However, some corporates acknowledge that the pandemic is a tipping point in this regard. "For many people, the pandemic has clarified the need for environmentally-friendly and socially-acceptable corporate activities," says one board member at a Swiss business. "Greater incorporation of environmental and social guidelines will be a major activist demand."

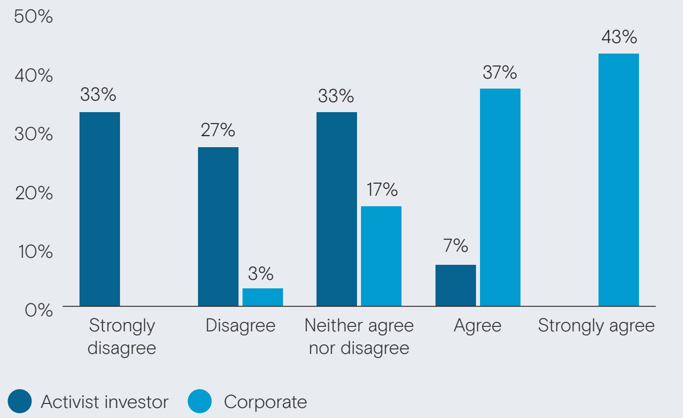
To what extent do you agree with the following statement: 'Activists will increasingly prioritise environmental, social and governance (ESG) issues in their campaign demands.'?



In your view, what are the most effective preventative measures that companies can use to mitigate the chances of activist campaigns?



Do you agree with the following statement: 'Increasing engagement between large, institutional investors and the companies in which they control major shareholdings will greatly diminish the role of activist investors.'



The virtue of transparency

It certainly appears that, while corporates do recognise the imperative to engage with shareholders (including activists), some are keen to keep them at arm's length. "Companies should closely observe activist trends and the major demands being laid down," says the CEO of a French corporate. "They should be proactive in ascertaining their goals and be more assertive with their financial strategies."

Other boards are more realistic about the need for direct contact that is both open and honest. "European companies should be highly concerned about the growing number of activist campaigns. If they can't answer investor queries in a transparent manner, they'll soon run into more problems," warns the CEO of a Swiss business. "Engagement strategies are the best way to ensure the smooth flow of ideas and insights, allowing investors to voice their opinions and feel more valuable," adds the CEO of an Italian company.

Still, while it is always good to talk, it also matters what you say and who you say it to. Some 80% of the corporate respondents to this research believe that increased engagement between companies and large, institutional investors is likely to diminish the role of activists. But this may be wishful thinking – 60% of activist investors disagree with this view, including 33% who strongly disagree.

The clash may reflect activists' discontent with what they hear from boards. Or it may signal resentment that corporates are focusing only on their largest investors and excluding activists from the conversation. Either way, the data suggests boards will need to think harder about how to maintain a constructive dialogue with all shareholders if they wish to avoid public campaigns.

> Engagement strategies are the best way to ensure the smooth flow of ideas. They allow investors to feel more valuable.
>
> CEO of an Italian Corporate

"Investment decisions and voting can be streamlined to a certain extent, but this will not diminish the role of activists," warns a partner and CIO of a UK-based activist. At a French corporate, the CEO agrees: "It will be very beneficial for companies to consider better engagement practices. If activists increase their influence in the absence of proper engagement, it could lead to forced decisions and negative results for the company."

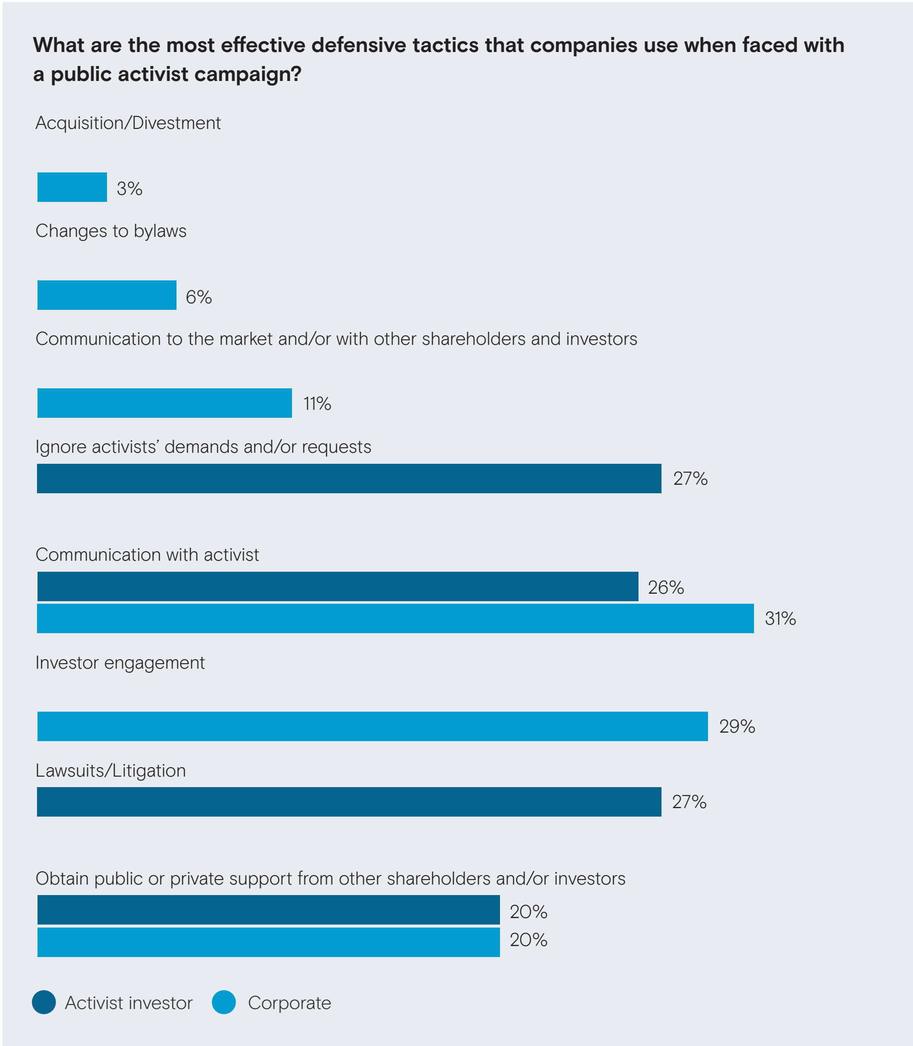
The key is to "bring the activist into the tent", suggests Skadden's Bruce Embley. "Have your decks ready. If an activist picks up the phone and says, 'We think you need to do this', you can say, 'That's really interesting – we actually talked about this recently and we would be really interested to get your insights'. That does take some of the heat out of a situation."

Flex your muscles
But what if these preventative tactics fail to curb the launch of a public campaign? Here, both sides agree it is important to keep talking: among corporates and activists surveyed, 31% and 26%, respectively, regard communication with the activist as an effective defensive tactic in such circumstances.

However, corporates should not expect these conversations to solve all their problems. Activists are ready to play hardball – and candidly warn corporates that they may need to do the same. More than a quarter of activists (27%) suggest that one effective defence for corporates might simply be to ignore the demands being made; the same share suggest legal action could be a productive tactic. Strikingly, not a single corporate respondent to this research takes either of these views.

Still, some corporates do accept that it is imperative to be seen to be talking with the activists. "Boards have to respond well to instances of visible activism," argues the CEO of a French corporate. "There is not much that can be done through passive discussions after a campaign goes public."

Getting on top of the particulars not just of the demands being made, but



> If things get ugly, you have to respond... Quite frankly, if things go too far, you show your muscles and you litigate.
>
> Armand Grumberg, Skadden

of the activist making them, is equally important. "Be prepared: I've seen a lot of success when corporates have very quickly worked out how the activist has acquired their interest and its dynamics," says Skadden's Bruce Embley. "If you're able to explain, for instance, that they're holding contracts for difference, you can make the case to other shareholders that they're not all in it together."

"The bottom line is that if things get ugly, you have to respond to an attack," argues Skadden's Armand Grumberg. "You have to respond publicly with as many arguments and data points as possible. And, quite frankly, if things go too far, you show your muscles and you litigate."

4 Reassessing the balance of power

Most participants in a dispute of course feel the odds are somehow stacked against them. Activists and corporate boards are no exception – both sides commonly argue the system does not work in their favour, pointing to legal constraints, regulatory issues and market structures as standing in the way of their preferred outcome.

This research reflects that idea of being the underdog. Asked where the balance of power lies in confrontations between them, 69% of corporates complain it is skewed towards activists, whereas 47% of activists see corporates as holding all the cards.

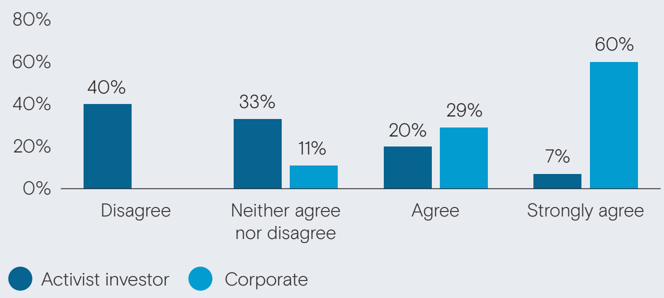
One might conclude that, in truth, the reality likely sits somewhere in the middle. And to be fair, 47% and 31% of activists and corporates, respectively, take the view that the balance of power between them is roughly equal. Nevertheless, elevated levels of activism and high-profile campaigns are likely to engender more debate about how that balance is managed – and whether reform is necessary.

The pandemic has already changed the dynamic in some ways. For example, while investors still have an opportunity to submit questions and raise issues at shareholder meetings, it has become more difficult to do so in some countries, with new regulation introduced to ease the orderly running of virtual company meetings.

Other changes are possible. The ongoing discussion about balancing the need for foreign direct investment with the importance of protecting domestic interests, particularly for companies deemed to be national assets, may precipitate legislation that makes life harder for activists. France has held tentative discussions about changes to financial market regulation in the context of investor activism.

Regarding the 'balance of power' between activists and companies, do you think it is roughly equal, or skewed more towards one side?

Do you expect and/or would you support an evolution of the legal framework with respect to activist investors and public campaigns over the next 12 months?



Appetite for reform

There is certainly some appetite for change, particularly among those on the receiving end of activism. Almost nine-in-10 corporates (89%) expect and support an evolution of the legal framework with respect to activist investors and public campaigns over the next 12 months. That figure includes 60% who feel strongly about this issue.

Activists are less persuaded, with 40% explicitly rejecting the idea that adjustments to the legal framework are necessary or desirable. Although 27% do understand the case for reform, it seems likely that activists fear any changes to the legislative backdrop would be to their disadvantage.

Certainly, corporates are keen to see measures that offer them greater protection. "The next 12 months will be crucial," says the CEO of a UK corporate. "Being a recovery period for many organisations, unnecessary disruptions caused by campaigns will negatively impact operations." In Italy, a board director adds: "As more public campaigns are being organised, it would be very useful to have a legal framework for adequate control. It will be reassuring for companies and investors alike."

In contrast, activists are anxious about what legal changes might mean for them. "Any evolution would totally disrupt campaigns and also won't produce any notable benefits for companies," argues the CEO and senior partner at an activist investor in Switzerland. "The current framework should be adhered to because it is a practical one." The CIO of a UK activist adds: "The current federal and state laws in regions are adequate and secure the rights of parties to oppose and defend in a systematic manner. There is no need for further evolution to take place."

Reconciling these views will be difficult. The question for policymakers is whether potentially elevated levels of shareholder activism make it imperative to consider reform, given the many pressing priorities as Europe seeks to bounce back from the pandemic. "An evolution is not useful right now," argues a partner of an Italian activist investor. "It would be better to concentrate on the recovery."

Skadden's Holger Hofmeister takes the same near-term view. "Everyone is really focused on just keeping things going and making sure the pandemic does not hold up everything," he points out. As Skadden's Armand Grumberg puts it, "There are just other emergencies to deal with right now."

Axioms on activism for mindful companies

Our research and discussions with corporates and investors alike point to an undeniable surge in activism in 2021. The pandemic has had a profound impact on every business. Activists are naturally determined to protect their interests, to focus on boards' responses to the crisis, and to exploit new opportunities.

Corporates must be prepared for this scrutiny. Those companies that fail to consider the threat of activist campaigns should not be surprised to find themselves caught out. They may discover, to their peril, that it is more difficult to prevent initial contact with activists developing into a full-blown public confrontation. Much better to have robust plans in place.

Part of the challenge is to understand the issues that will motivate activists over the next 12 months. Their focus on board independence and dividend policy is understandable given the market backdrop. Corporates should be asking themselves some searching questions about these issues.

Equally, boards must work hard to engage meaningfully with shareholders – and not only the largest institutions. Early contact with activists and a willingness to listen will give boards a much better chance of heading off a potentially nasty confrontation.

Clearly, it will not always be possible to meet activists' demands, even where boards accept action may be in the interests of the broader shareholder base. Commercial realities may make it challenging to restore dividend payments in the short term. M&A opportunities may not be forthcoming. Even so, boards should be ready to expound on their longer-term plans.

Some matters are too pressing to defer. Activists' growing interest in ESG issues is part of a broader surge in the importance of such matters, with policymakers, customers, employees and suppliers among other key stakeholder groups looking for credible board responses. "Climate change cannot be ignored, nor can concerns about lack of diversity in the workplace," as the managing director of a German activist puts it.

The bottom line is that the challenge posed by activists will not recede any time soon. However, well-prepared boards that are comfortable engaging with activists and have a compelling narrative with which to respond to their demands are very well-placed to mitigate risk.

Key takeaways:

1. Don't panic. Though key markets and industries should expect to face an increased number of activist demands in the coming months, most activists surveyed are not, currently at least, considering launching major public campaigns in Europe in 2021. Companies should focus on their fundamentals, assess and mitigate their potential vulnerabilities, remain responsive to shareholders, anticipate demands and new focuses such as ESG, and be open to private dialogues with investors.

2. Don't shut the door. Engaging with regular sets of advisers and other third parties can help companies to mitigate or anticipate activism. This will be particularly useful for companies that have not analysed the possibility of being approached by activists in the near future. Such measures should be supplemented with a continuing development of transparency, clarity and promotion of engagement with all shareholders. Confidence with the board will be crucial, especially in the face of economic uncertainty. In any event, if approached by activists, companies should not immediately shut the door to discussions.

3. Don't be afraid to put up a fight. If an activist opts to take a campaign public and/or uses "dirty tricks", one potentially effective course of action is to "ignore" their demands, provided the company monitors closely the actions taken by such activists, remains in constant interaction with its long-term shareholders, communicates regularly to the market in full transparency, and is fully prepared to take the subsequent measures that may be required. Depending on the campaign, going to court quickly may be a serious option for a company wishing to react and defend itself efficiently.

About Skadden

Skadden is a global leader among law firms involved in mergers and acquisitions and other corporate transactions, and a top adviser for clients on corporate governance, takeover preparedness, contests for corporate control, proxy fights, and other forms of shareholder activism. We provide clients with an integrated team from different areas of law, including attorneys from our M&A, corporate governance, and litigation practices. Our diversity of experience helps clients address the full spectrum of issues presented by activists and is key to helping our clients prepare for and respond to activist shareholders advocating strategic, financial, or structural changes.

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About Activistmonitor

Activistmonitor delivers a unique combination of in-depth reporting and historical analysis on key activist campaigns for advisors and the investment community. Our quick and comprehensive news service provides the backbone for analytical tools which allow you to anticipate the next move in an activist campaign or generate new business ideas based on active investing trends in the marketplace.

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