ACTIVIST INVESTING IN EUROPE

2018

Activist Insight

Skadden

THE TEAM

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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ACTIVISM IN EUROPE

Josh Black, Activist Insight.

WHETHER through lack of opportunities in the U.S. or an unusually appealing economic climate, Europe came to the fore in activism during 2018. According to *Activist Insight Online* data, the $7.6 billion of newly disclosed activist investments in Europe during the first quarter was the biggest start to a year since 2015 and only the third quarter in which the value of new activist stakes was higher in Europe than in the U.S. since 2013.

The number of activist campaigns may not be growing, however. At the end of the third quarter, activity in four of the five markets covered in-depth by this report had fallen compared to the same period last year.

Then again, those countries accounted for just over half of the total number of situations in Europe tracked by *Activist Insight Online*. The likes of Poland, Slovenia, and Czechia have activist cultures, if not yet a great deal of attention from traditional activists. Although the strength of the U.K. activism market stands out, the allocation of significant resources to the Continent should not be overlooked.

Three themes stand out from 2018's experience. First, the appeal of European and specifically U.K.-listed assets to American buyers. The likes of Whitbread, SodaStream, and Sky sold themselves or business divisions to U.S. buyers in the first nine months of the year, while the number of U.K.-based companies subjected to public demands by U.S.-based activists has doubled from 2017 to 2018.

Second, the fulfillment of a prediction made in last year's *Activist Investing in Europe* report, when we wrote that "U.S. activist interest in Europe has increased and the groundwork has been laid for a sustained level of activism." ValueAct Capital Partners now has three significant investments in the U.K., including the only non-U.S. stake in its impact investing fund, while Trian Partners raised 270 million pounds through the London Stock Exchange for what may be a U.K. target.

Third, the big campaigns have been less event-driven and more operational in nature. Non-European-based activists are more likely to push for M&A-related demands, a fact that was in evidence last year at Clariant and AkzoNobel. But ValueAct and Trian are known for their operational focus, while the year's biggest headlines were generated by Elliott Management's proxy contest at Telecom Italia, where the Italian government intervened to prevent asset sales. ThyssenKrupp, where Elliott and Cevian Capital pushed for a looser conglomerate structure, was more complicated than a mere breakup play, even though the interim CEO ultimately fell behind a plan to split the business in two.

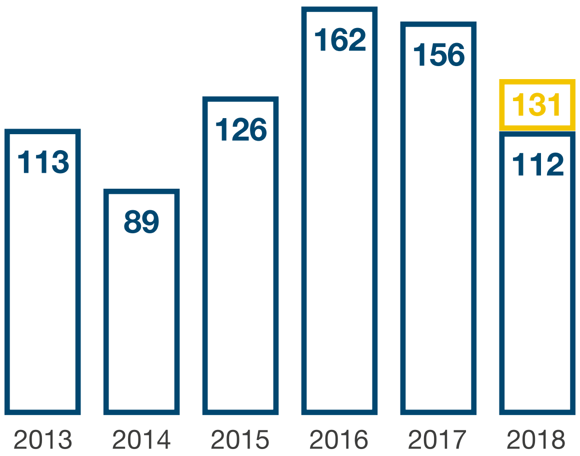
Nonetheless, this year looks set to exceed 2017's level of public demands for M&A to take place, with 17 recorded in the first three quarters of this year versus 15 in the same period last year. Opposition to M&A, often enabled by favorable minority protections, has melted away, falling from 15 in the first three quarters of 2017 to eight in 2018 thus far. European investors are reaping the advantages of a strong dollar and the deployment of private equity capital.

More broadly, institutional investors continue to be vocal even outside of boardrooms and collective action vehicles such as The Investor Forum. At Unilever, Aviva, and Ryanair, individual institutions have offered public criticisms. At Sports Direct, pressure finally led to board changes, while Unilever scrapped a plan to reincorporate solely in the Netherlands amid fears it would disadvantage U.K. institutional investors. Whether this trend spreads to the Continent, where the players are substantially different, will be a big question for 2019.

Thanks in no small part to the rising profile of activism in Europe, we have been able to expand this report and hope it will become the pre-eminent annual survey of the topic. We are grateful for the support of Skadden, our partners for a fourth time, as well as new contributors Georgeson, Morgan Stanley, and Brunswick.

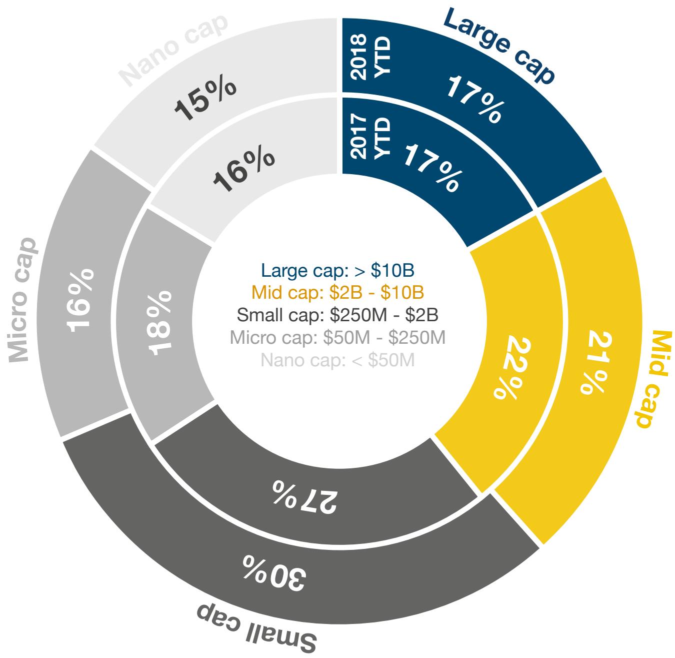
> “Institutional investors continue to be vocal even outside of boardrooms and collective action vehicles such as The Investor Forum.”

European targets by year



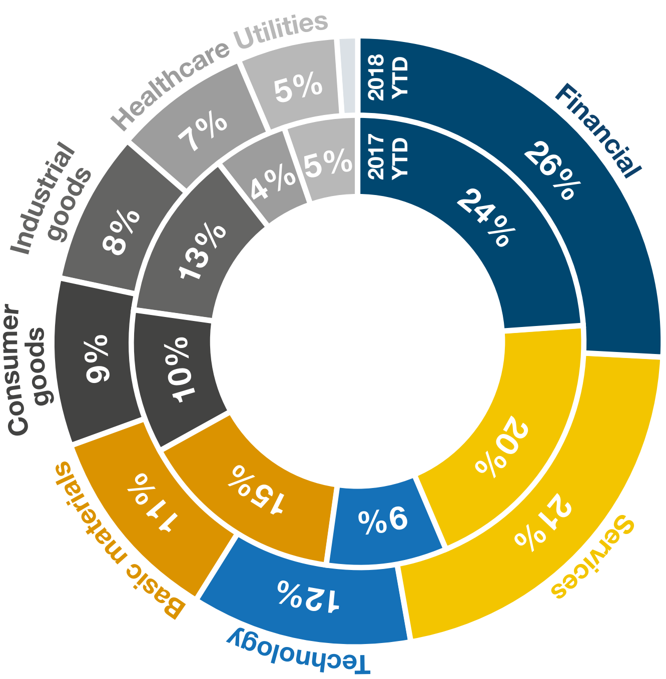
Number of Europe-based companies publicly subjected to activist demands. 2018 data as of Sep 30. Figure in yellow box is a projected 2018 full year figure.

European targets by market cap



Market cap breakdown of Europe-based companies publicly subjected to activist demands between Jan 1, 2017 and Sep 30, 2017, and Jan 1, 2018 and Sep 30, 2018.
Note: Rounding may lead to summation errors.

European targets by sector



Sector breakdown of Europe-based companies publicly subjected to activist demands between Jan 1, 2017 and Sep 30, 2017, and Jan 1, 2018 and Sep 30, 2018.
Note: Rounding may lead to summation errors.

48%

Proportion of resolved public activist demands at Europe-based companies at least partially satisfied.

447

Number of board seats gained by activist nominees at Europe-based companies since 2014.

28

Number of Europe-based companies publicly subjected to **Amber Capital’s** activist demands since 2013.

COUNTRY PROFILE

UNITED KINGDOM

Eleanor O'Donnell, Activist Insight.

AS activists have flocked across the pond from America this year, activism in the U.K. has risen compared to 2017, with higher levels of interest in the financial sector and a harder push for M&A, according to data curated by Activist Insight.

Even traditional investors have started to take a more active approach to counter a lack of communication between board members and shareholders. Discontent over Unilever's proposed reincorporation as a solely Dutch company highlights the potential for flashpoints.

Bess Joffe of advisory firm SquareWell Partners told Activist Insight, "most U.K. corporates only speak to their top 10-15 [shareholders] and to proxy advisers but they need to find more efficient ways to communicate more widely to their shareholders and defend their strategy and ESG [environmental, social and governance] practices…or risk being surprised by some of the market expectations."

Michael Henson, a partner and co-founder of Statera Partners, sees this lack of communication creating an opening for activists to step in with ready-made support. In this environment, "even activists least known to, or trusted by, the U.K. institutional investor community can exert pressure and have a destabilizing influence on companies," he says. "They create the environment where more established funds can take a position and unlock investor support. Due to this dynamic, we caution companies against being dismissive or complacent in their dealings with a broad range of investors."

Banknote manufacturer De La Rue was attacked by Crystal Amber this year after a major contract loss. Frustration with De La Rue's board led Crystal Amber to urge the company to come up with a viable strategy and expand by continuing its focus on cutting-edge technology. The activist investor's founder, Richard Bernstein, said De La Rue shareholders "do not buy the company's growth messaging and strategy."

This type of shareholder dissatisfaction, coupled with the ten-year anniversary of the financial crisis, means shareholders "are starting to consider major re-examinations of the structure of executive compensation," Joffe's colleague Louis Barbier says. The Investment Association has been adding significant opposition votes to its online public register, increasing the scrutiny on controversial issuers.

A weaker pound may increase the sense of opportunity for activists. "With the fall in value of the pound, the U.K. looks cheap to investors and we may see continued volatility as Brexit continues to wind its way down the path," Barbier believes.

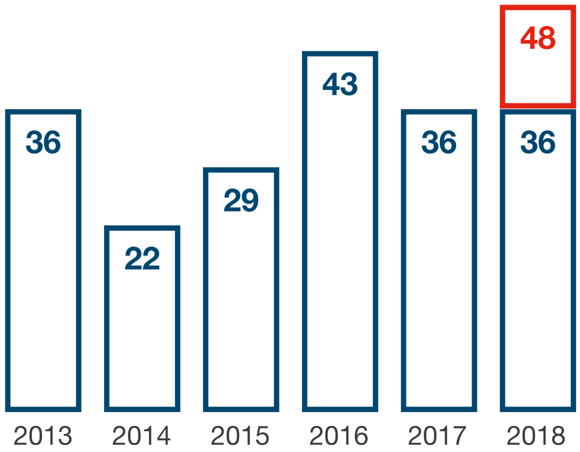
ValueAct Capital Partners is among those that took advantage of the situation this year, with multiple U.K. investments including Merlin Entertainments and Horizon Discovery Group, the latter through a new impact investing fund. ValueAct bought into Horizon only months after the company rejected a takeover bid from life science e-commerce company Abcam as too low in May and is pushing for a seat on Horizon's board. There have also been rumors that Trian Partners, one of the most-feared activists, raised 270 million pounds for a potential investment in a U.K. company.

Although co-founder and CEO of Charity & Investment Asset Management (CIAM) Catherine Berjal sees "an increasing reluctance from companies to invest in the U.K. in the lead up to Brexit," she admits that "these events can also open up opportunities."

Indeed, one of the year's big inbound deals saw Twenty-First Century Fox and Comcast fighting over Sky while Odey Asset Management and Elliott Management agitated for a higher price – the latter retaining investment bank Greenhill to make its case to the U.K. Takeover Panel.

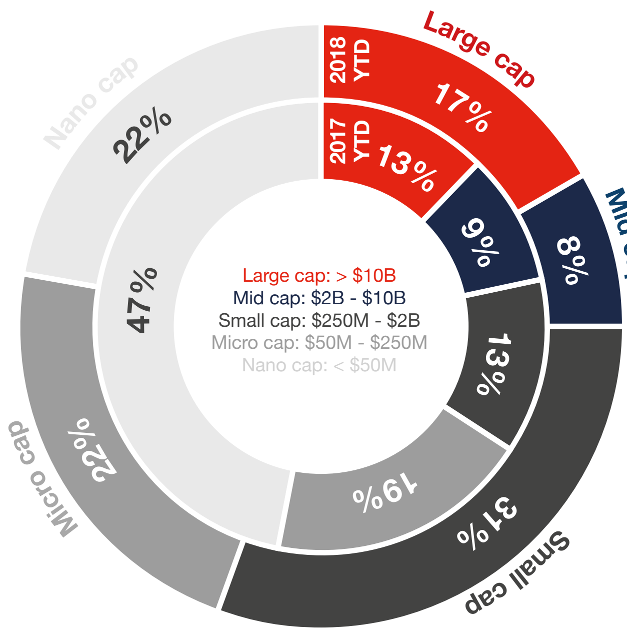
Gatemore Capital Management Managing Partner Liad Meidar meanwhile sees "more information scarcity, especially with small cap equities, largely as a result of smaller research houses getting cut off from investors." If Brexit is softer than anticipated, activists in the U.K. are primed to take advantage of a rebound in both the currency and in stock prices.

U.K. targets by year



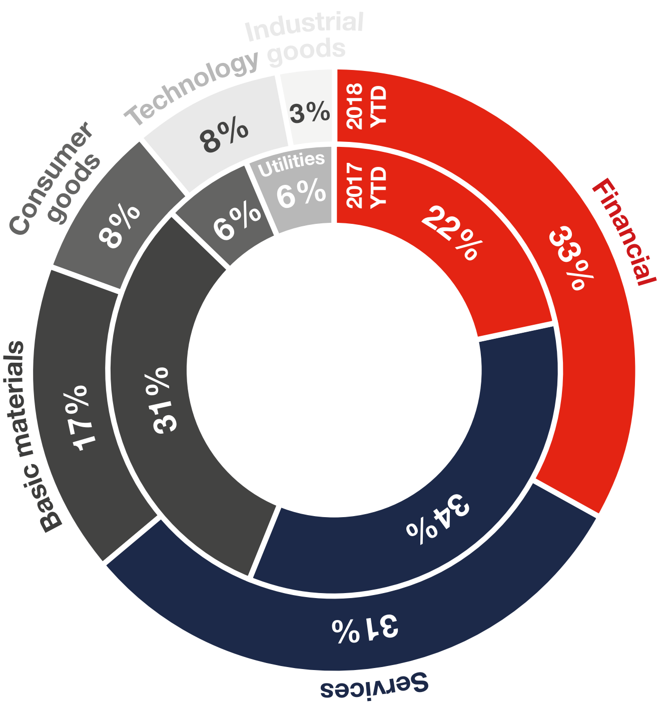
Number of U.K.-based companies publicly subjected to activist demands. 2018 data as of Sep 30. Figure in red box is a projected 2018 full year figure.

U.K. targets by market cap



Market cap breakdown of U.K.-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

U.K. targets by sector



Sector breakdown of U.K.-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

54%

Proportion of resolved public activist demands at U.K.-based companies at least partially satisfied.

91

Number of board seats gained by activist nominees at U.K.-based companies since 2014.

13

Number of U.K.-based companies publicly subjected to **Harwood Capital's** activist demands since 2013.

LEGAL ANALYSIS
UNITED KINGDOM

Scott Hopkins, Skadden.

THE prospect of Brexit continues to create uncertainty for companies and investors alike in the U.K. and Europe, as it remains to be seen what form any deal between the U.K. government and the European Union will take – or, indeed, if there will be one. However, shareholder activism continues to be prevalent. Once again, the U.K. provided the lion's share of opportunities in Europe for activist investors, with 21 out of 40 reported campaigns targeting U.K. companies.

Activist investors have continued to embrace a broad range of campaign objectives, primarily focused on board changes and M&A, but there has also been an increased focus on governance-driven activism, reflecting a changing political and regulatory landscape that favors investor engagement.

Board-focused activism has continued to form the backbone of U.K. campaigns in 2018, with over half of public campaigns to date concerned with board issues. It has, however, met with mixed success. Following a campaign by Renova last year to oust Petropavlovsk's co-founder Peter Hambro and several other directors, the company announced in September that Hambro would be returning as president and senior adviser to the board – a sure reminder to activist investors that not all changes are permanent.

2018 has been one of the most significant and successful years so far for event-driven activism in the U.K. in light of the high-profile takeover battle between Comcast and Fox-Disney for Sky. The outcome of this long, drawn-out takeover battle is encouraging for activist investors and means that we are likely to see more event-driven activism going forward.

A further theme that has been evident in 2018 is the emergence of activist investors encouraging public company carve-outs of operating businesses that represent attractive targets to potential investors, particularly in the private equity arena. In July, Micro Focus announced the sale of its German software business for $2.5 billion to private equity fund EQT Partners. Elliott Management held a 5.1% stake in Micro Focus, although it was not publicly connected to the transaction. In August, Elliott and Sachem Head succeeded in their push for the demerger of Whitbread and Costa Coffee, which will be sold to Coca-Cola for 3.9 billion pounds. The combination of acquisitive private equity investors and increased shareholder activism may provide more opportunities for these kinds of transactions in 2019.

Updates to the U.K. Corporate Governance Code, the implementation of the European Shareholder Rights Directive II and an expected update to the 2012 U.K. Stewardship Code will likely lead to an opportunity for activist investors to seek to implement long-term strategies focused around rising environmental, social and governance (ESG) concerns, a trend which has already been seen in 2018.

In March, activist investors at Royal Dutch Shell continued to put pressure on the company to set tougher emissions targets in line with the Paris Agreement. Although the resolution was defeated at Shell's annual meeting, about half of investors' questions related to climate change. In May, Legal and General announced that it had launched the first gender-oriented fund to focus exclusively on U.K.-listed companies, aiming to improve diversity standards at a specially selected group of 350 companies.

The U.K.'s legal, regulatory and political landscape remains supportive of shareholder engagement. However, increasing demands for long-term engagement as "stewardship" rather than short-term value creation may cause tensions to arise between the current activist model and the regulatory and social environment in which it operates. How activist investors keep pace with, and adapt to, this trend in the U.K. will be interesting to watch.

> "Activist investors, particularly those with a penchant for arbitrage, will be encouraged by the outcome of the Sky saga."

An interview with Scott Hopkins.

Is the level of activism in the public eye indicative of the volume of activism behind-the-scenes?

There is a school of thought that the most successful activist campaigns are those conducted behind closed doors. However, increased levels of publicly reported activism are a good indicator of healthy volumes of activity more generally. Across Europe, the number of companies publicly subjected to activist demands is down from 2017 (but up in the U.K.). We can ponder the reasons for a decline in activist campaigns in Europe reaching the papers, but we question whether this indicates a decline in levels of activist campaigns, given the increased levels in the U.K.

With the introduction of standstill agreements, have U.K. companies become more comfortable adding an activist to their board?

The use of standstill agreements, coupled with other constraints imposed on shareholder-nominated directors, such as information policies and procedures to manage conflicts of interest, have provided companies with greater levels of comfort when faced with the prospect of an activist-nominated director being appointed to the board. Entry into a standstill agreement is generally seen as a quid pro quo for increased access to information that nominated directors are exposed to, which it is assumed is passed back to the activist.

Does the U.K. Takeover Panel decision regarding Sky increase the likelihood of arbitrage activism?

Absolutely. We expect that the panel's decision on Sky to require a "chain-principle mandatory bid" and the ensuing bidding war that culminated in the normal, Takeover Code-governed auction process will embolden arbitrageurs. The delta between Fox's opening offer price of 10.75 pounds per share and the ultimate price of 17.28 pounds paid by Comcast demonstrates the ability of activists to capture increased shareholder returns in competitive bid scenarios. Activist investors, particularly those with a penchant for arbitrage, will be encouraged by the outcome of this saga and we expect to see more event-driven activism going forward. We believe the result may also cause traditional institutional investors to consider whether they left money on the table by selling out too early.

Are major government-backed corporate governance reforms off the table for good?

The U.K. corporate governance regime is widely regarded as the "gold standard," but initiatives backed by the U.K. government continue to drive change and improvement; the corporate governance landscape is constantly evolving.

The publication of a revised U.K. Corporate Governance Code in July 2018 (the "Revised Code"), which will come into effect on January 1, 2019, was the product of a thorough review conducted by the U.K. Financial Reporting Council, set against the backdrop of the House of Commons Business, Energy and Industrial Strategy Committee and a government green paper focused on corporate governance issues. Such initiatives are indicative of the use of legislation as a tool to improve standards and promote change.

In particular, the Revised Code encourages shareholders to scrutinize boards and hold directors to account. Reading between the lines of the reports accompanying such initiatives, further reforms should be expected if shareholders do not rise to this challenge, or if boards fail to more actively engage with key stakeholders.

How is the Shareholder Rights Directive affecting corporate governance in the country?

Company law and corporate governance practices in the U.K. already embody many of the requirements of the directive, but it is expected that these will be updated to remain in line with the directive. Certain of the obligations relevant to institutional investors and asset managers are imposed on a "comply or explain" basis, and are more specific and restrictive than the equivalent obligations currently in place under the U.K. Stewardship Code (2012). It is likely that updates to English law and corporate governance practices to ensure parity with the Shareholder Rights Directive will continue to encourage and foster increasingly meaningful engagement by shareholders.

BEHIND THE ACTIVIST CURTAIN

Cas Sydorowitz, Global Head of Activism at Georgeson.

When an activist declares a disclosable position in a company it doesn't just happen by accident. The process and timing are well-planned.

Most activists have a very concentrated portfolio with some having as few as three-to-four positions, so announcing what stock has been added to that elite portfolio is newsworthy beyond its relevance to the company.

Nothing left to chance

Long before the activist discloses its holding, it has stress-tested the investment thesis on the company in question extensively. Its ability to demonstrate success to its own clients while protecting its reputation is paramount. Its determination to proceed with a campaign must contain a clear path to success. There will be value upside, levers to pull to create that value and an exit strategy.

To get to this point the activist will have invested several man-years of research on the company in question. That includes speaking to other shareholders, customers, suppliers, current and former employees and directors, and market peers. Some activists will meet with management even before they take a position to assess whether the management will be amenable to their suggestions or resist their ideas outright.

Deep research

To demonstrate to the board that they know this company inside out and perhaps better than directors do, activists go to extraordinary lengths to understand what is keeping the company from realizing its potential, and what changes need to happen to unlock that value. The research is done from an "outside-in" perspective and will often be more comprehensive than the directors are being provided with by management, even though that is provided from within the company.

To purchase a stake activists need to define a price band, working with various brokers who will not leak that they are accumulating a stake. The last thing the shareholder wants is to have the price run away from it before it can accumulate its position. This process may take some time, unless it can purchase the shares from another shareholder.

A new standard

It is no longer necessary to have a 5-10% stake to apply pressure on the board to initiate change. Activists have become far more adept at building a wider consensus among other shareholders and stakeholders to get the board to change. The threat of a protracted, drawn-out proxy fight can be enough to get boards to the table, especially in the face of the army of advisers that the activist will bring to the campaign.

To achieve their objective, activists will seek out support from local counsel to ensure they understand the rights they have as shareholders and what recourse they can take to achieve their objective. They will usually hire their own local PR firm to add pressure through local and international media. Board members will face questions and criticism from their peers, family and friends that they have read in the press. Among the other advisers, proxy solicitors will help them mobilize support from other shareholders.

Activists come into battle fully-prepared, having done extensive research on the company, the directors, the industry and the market. They are armed with the best advisers to support their efforts to unlock change. Companies can reject their suggestions outright, but that would ignore free, private equity-style analysis which has been done to create shareholder value. Activists are powerful opponents; issuers need to be even smarter and better prepared if they want to succeed.


Cover your king.
Georgeson's experience, insights and resources will deliver the winning moves.
CERTAINTY
INGENUITY
ADVANTAGE
Georgeson

COUNTRY PROFILE
FRANCE

Elana Duré, Activist Insight.

LEVELS of activist activity in France have fallen to their lowest levels since 2014, when only two companies were publicly subjected to new activist demands, with just four companies targeted as of September 30, down from eight in the same period last year.

Anne-Sophie d'Andlau, CEO of Paris-based Charity Investment Asset Management (CIAM), told Activist Insight that French culture has created a barrier for activists, prompting international firms to seek value elsewhere. She said there is a sort of brotherhood among corporate managers and directors, allowing executives to easily gain control of the boards. "Getting a hold of the network is difficult to crack," d'Andlau noted. "It's more difficult to tackle French markets."

Guy Wyser-Pratte echoed d'Andlau's sentiment, adding that the language barrier can also put international activists at "a great disadvantage," especially if the foreigners are considered corporate enemies.

In May, Sterling Strategic Value and Financière De l'Echiquier built 3% stakes in French aerospace company Latécoère, seeking board representation. Elliott Management also returned to controlled company XPO Logistics Europe, hoping to change the company's dividend policy and gain one board seat. All three failed in their initiatives.

Meanwhile, the loudest campaign of the year was waged by London-based Amber Capital, to elect two directors to the board of publishing company Lagardère. At the time, Amber contended that Lagardère needed an injection of new skills and perspective to successfully restructure its active division, undertake a strategic review of its sports and entertainment units, and improve its free cash flow generation. Again, the activist failed to gain board representation.

Only Nokomis Capital gained a board seat at Sequans Communications in June, months after it entered a standstill accord with the company. The firm first built its stake in Sequans in November last year, but like other activists, had some unfinished business that rolled into the new year.

Wyser-Pratte's eponymous investment fund is currently engrossed in a court battle with Paris-based Viktoria Invest. The activist accused company insiders of trying to siphon off some of the firm's assets, but progress has been long and tedious because the French legal system is not straightforward, especially regarding minority shareholder rights. "The French establishment doesn't like what we do so they try to put obstacles in our way," Wyser-Pratte told Activist Insight. "We constantly have to be looking over our shoulders for what [they] are trying to do to try to stop us from improving shareholder value."

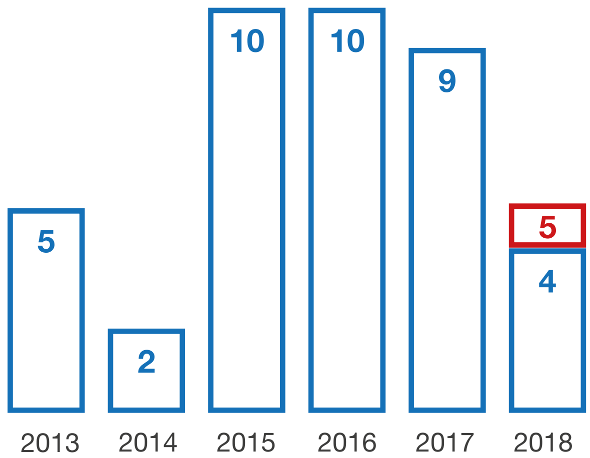
D'Andlau, however, thinks progress can be made so long as activists follow protocol and act without hostility. "We think the best style is to be as least aggressive as possible," d'Andlau explained. "We think the style is to be more engaging and really be seen as an active investor instead of an activist investor, which has a negative connotation."

CIAM recently criticized French insurance company Scor for hastily rejecting an unsolicited takeover proposal from its largest shareholder, Covéa. The activist contended the 43 euro per share offer is a premium to the company's historical share price. Scor, however, characterized CIAM as "a short-term disrupter in it to make money in a long-term value-creating business."

D'Andlau admitted that hurdles to gaining board representation exist, including the tendency of big shareholders to vote with management. "There has been little interest by institutional investors to really tackle corporate governance," she said, noting that it is an activist's duty to educate shareholders on its importance. "It's more difficult to convince these big shareholders to vote for a new board member even though it may better the board. We see things improving a bit, though."

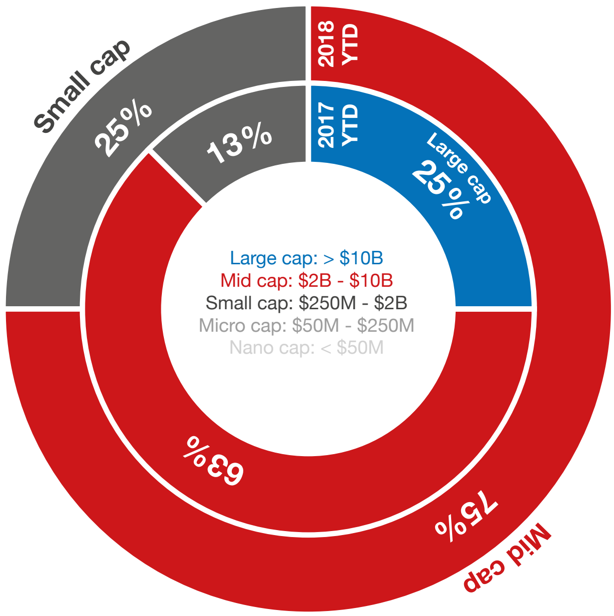
Regardless, 2018's low levels of activism are not indicative of a decline in the region, but rather slow growth. Swedish firm Cevian Capital made its first investment in France two years ago when it built a stake in electricity provider Rexel and d'Andlau is confident others will follow suit in due time. "It's going to grow, there's no turnaround," she said.

French targets by year



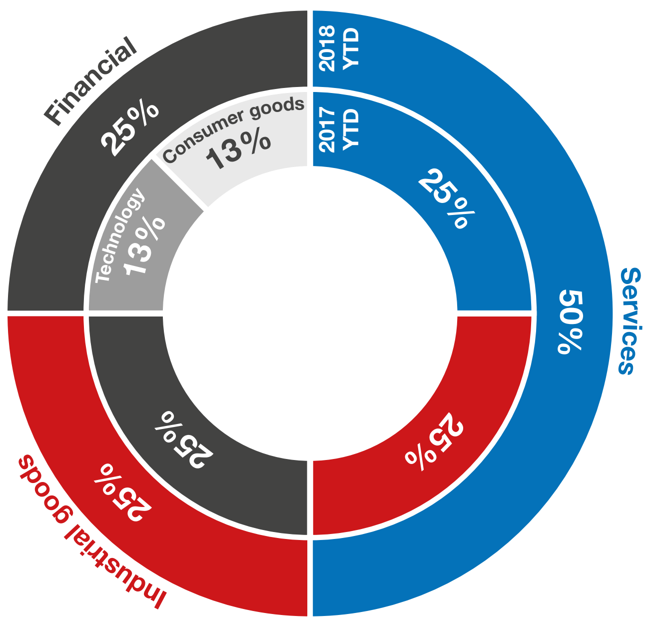
Number of France-based companies publicly subjected to activist demands. 2018 data as of Sep 30, 2018. Figure in red box is a projected 2018 figure.

French targets by market cap



Market cap breakdown of France-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

French targets by sector



Sector breakdown of France-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

32%

Proportion of resolved public activist demands at France-based companies at least partially satisfied.

12

Number of board seats gained by activist nominees at France-based companies since 2014.

5

Number of France-based companies publicly subjected to **Charity Investment Asset Management's (CIAM)** activist demands since 2013.

LEGAL ANALYSIS
FRANCE

Armand Grumberg and François Barrière, Skadden.

CORPORATE governance rules and best practices have accompanied the development of shareholder activism in France during the past years. The steady increase of shareholder campaigns in France and Continental Europe in recent years has led public authorities to provide a legal framework addressing such issues. The main purpose is to avoid short-term value-driven activism in favor of long-term investments.

The recent investment of CIAM, known for having initiated a number of activist campaigns, in Scor, one of the world's leading reinsurance companies, a few days after the decision of Scor's board of directors to reject an unsolicited public takeover proposal was made public, is a prime example of a short-term speculative investment with an activist intent.

In connection with the development of shareholder activism, French and European legislators have generally followed a trend leading to further involvement of shareholders and a strengthening of their rights. Directive (EU) 2017/828 dated May 17, 2017, encouraging long-term shareholder engagement was adopted, providing in particular for greater transparency in the decision-making process between issuers and investors. Among other things, the directive provides that:

• Asset managers and institutional investors should publish a shareholder engagement policy, including their role as shareholders within their long-term investment strategy;

• Proxy advisers should publish their code of conduct and the research undertaken before recommending votes, as well as conflicts of interest;

• Companies should publish on their website the related-parties transactions subject to approval from the board and the shareholders.

The directive is currently being transposed into French law by the so-called PACTE Act, a bill which is currently the subject of well-advanced discussions at the French Parliament. The transposition will in principle slightly amend French provisions relating to shareholder engagement policy for asset managers and institutional investors, or with regard to related-party transactions, as French law already provides for a series of provisions to that effect. The PACTE Act should in particular create a new obligation for listed companies to publish such related-party transactions.

Regarding the code of conduct of proxy advisers, the rules and regulations are, to date, only governed by recommendations of the AMF, the French Financial Market Authority, and the PACTE Act is expected to introduce a new set of legislative rules applicable to proxy advisers, although they would to a large extent be similar to the current AMF recommendations.

In addition, the draft of the PACTE Act contemplates lowering the threshold for a squeeze-out from 95% to 90% of the capital and voting rights owned by a controlling shareholder. The consequence of this provision, if enacted, would be to increase the difficulty for activists to block a squeeze-out and thus request a resale premium in the event of a takeover bid. In the past, Elliott Management was able to successfully block the squeeze-out of XPO Logistics Europe (formerly Norbert Dentressangle).

XPO Logistics obtained an 86.2% stake in XPO Logistics Europe after its public tender offer in 2015 and tried to acquire additional shares to reach the 95% threshold to launch a squeeze-out. Given Elliott's ownership of a 7.9% stake, XPO Logistics. has been, and still is, prevented from doing so. More generally, in France, between 2015 and 2017, 12 bidders which stated an intention to implement a mandatory squeeze out after their successful public tender offers did not reach the 95% threshold, although approximately half of these did reach the 90% threshold and therefore could have implemented a squeeze-out had the threshold been lower.

"French-listed companies have understood that they are now under the scrutiny of activists and that they have to maintain a high level of corporate governance."

An interview with Armand Grumberg and François Barrière.

Is the level of activism in the public eye indicative of the volume of activism behind-the-scenes?

The French practice – except for M&A activism – generally is for influential shareholders to first engage in longer confidential interactions with the board and management before launching a public campaign, and to launch such a public campaign only when discussions have failed. Therefore, the number of activist demands is far more significant than the number of public campaigns.

Are French companies under pressure to separate the chairman and CEO roles?

In the past, there has been significant pressure to separate the roles of chairman and CEO. This has led to the effective separation of such roles in a number of French-listed companies. However, this trend has changed, and at this stage, neither shareholders nor activists seem to focus primarily on this matter.

Has executive remuneration continued to be problematic for French boards?

While the general meeting and reporting documentation of Carrefour recently highlighted problems relating to certain compensation issues (see below), French boards have largely avoided criticism of executive compensation. Executive compensation has been widely approved with rates above 90% in the majority of the resolutions presented to the shareholders, and only in very rare circumstances have shareholders raised public questions regarding compensation issues to the boards of the French-listed companies composing the CAC40.

How is the Shareholder Rights Directive affecting corporate governance in the country?

The Shareholder Rights Directive's (SRD) national transposition is currently being discussed, so its effects are yet to be seen. France already adopted in 2016 a binding shareholders "say on pay" vote on executive compensation, which is one of the principal points of improvement of the SRD. The draft transposition law incorporates a number of transparency aspects: it creates means for shareholders to follow up on the proxies they grant, and it sets obligations for institutional investors and funds to publish their investment strategy and the way it relates to their long-term commitments as shareholders. Related-party transactions rules are also expected to be amended (e.g., where a related-party will have to abstain from participating in the discussions – not just the vote).

Has the annual reporting requirement around corporate governance led to pressure from investors for reforms?

Annual reporting has led investors to be more sensitive to specific situations, such as executive compensation. For example, the severance package of Carrefour's chairman and CEO, which was questioned by investors in June 2018, has led the AFEP-MEDEF to amend its Corporate Governance Code by providing for a stricter framework on officers' compensation, including an age limit of 65 years for the payment of a non-compete benefit, as well as the impossibility of executing such an agreement at the time of the officer's departure.

There has been less M&A activism in France this year. What accounts for the difference?

This year's M&A activism demands have slightly decreased from previous years. French-listed companies have understood that they are now under the scrutiny of activists and that they have to maintain a high level of corporate governance, including in connection with M&A transactions. French companies are now more aware and able to maintain open discussions with their shareholders to avoid any public demands and battles with activists. However, CIAM's public statements relating to Scor's rejection of Covéa's unsolicited takeover proposal indicate that M&A activism may arise at any time.

WHY GOOD COMMUNICATION IS KEY

Amelia Pan, Partner at Brunswick.

There was a time when European companies didn't worry much about activist investors. They thought long history, high status and protective local regulations would protect them.

That changed with AkzoNobel, Rolls-Royce, Nestlé, Danone and Shire, which demonstrated how U.S. activism could work here. Now "homegrown" activists such as Cevian, CIAM, and The Children's Investment Fund ("TCI") have launched big campaigns of their own to unlock shareholder value across Europe.

Two important trends guarantee there will be more. First, capital flows have gone global and company share registers are now dominated by funds like BlackRock, Vanguard, and Fidelity. Their U.S. heritage and experience make them more likely to support activist campaigns. Second, the reputation of activists has changed: some corporate raiders are getting support from the public and other shareholders.

Talk to them

European companies can learn from their American peers, not least how communications can shape the outcome of an activist campaign. It's no longer enough to react with defensive crisis communications. Engaging with the activist quickly, respectfully and constructively is an opportunity to avoid major disruption and preserve management control.

Those who choose to ignore an activist's proposal may be surprised by the support the activist receives from other large shareholders. When Brunswick surveyed global fund managers, 75% of those who responded felt activism was a force for good.

European media have not entirely bought into the nice guy activist thesis: they still tend to see them as overly challenging and even disrespectful. In response, activists have adopted a more cooperative, less aggressive approach. They have largely kept their proposals out of the media and have positioned themselves as advisers and supporters of the companies and creators of long-term value.

Management and boards must take any focus on corporate governance and strategy seriously and analyze and respond to potential points of attack. Communications aligned with a company's previously announced strategies are key to ensuring messaging aimed at internal and external stakeholders conveys a sense of business as usual. In addition to regular CEO/CFO meetings, they need to deploy their independent directors in discussions with investors - listening to concerns, communicating strategic priorities, and strengthening the relationship between the investor and the company.

Use every channel

Activists have developed sophisticated social media campaigns to reach their target audience in real time and gain support. Using links embedded within digital communications, they drive traffic to dedicated campaign websites ("microsites") and use graphics and videos to help maximize engagement with shareholders. Search engine optimization and paid advertisements help target key audiences.

In response, companies must look beyond traditional semi-annual investor roadshows and traditional media outlets and ensure that they have a dynamic and responsive communications infrastructure in place.

Constant shareholder communication and shareholder management are key. Today's investors receive company news through digital and social media channels - according to Brunswick research, 90% of fund managers scan LinkedIn, Twitter or Google when researching a company to monitor the chatter around a company and follow journalists who might post scoops online.

A company that communicates consistently across all channels ensures that its long-term business strategy is understood and creates a stronger alignment with investors.

Start early, win fast

Look at everything you are doing now, applying the gaze of an activist. Don't wait for the knock on the door: make sure the shareholders have the story already. And if the activists do come, you may be able to avoid a costly campaign by engaging from the start.

THE KEY CAMPAIGNS IN 2018

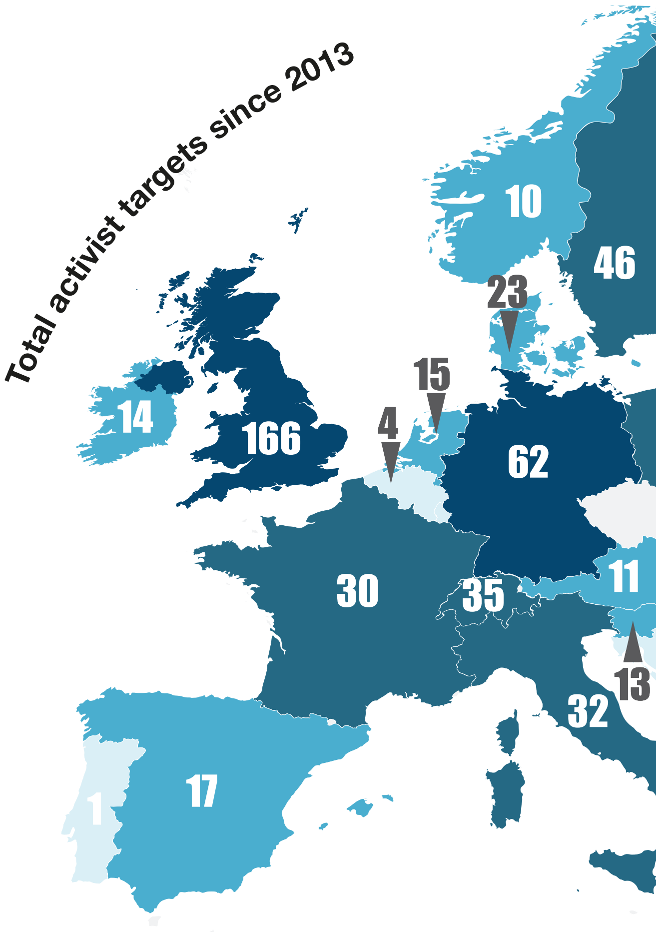
ACTIVISM IN EUROPE

United Kingdom

Elliott Management at Sky
ValueAct Capital Management at Discovery Group
Institutional investors at Unilever

Italy

Elliott Management at Telecom Italia
Shareholder Value Management at Retelit
Dennis Dumont at Credito Valtellinese



Germany

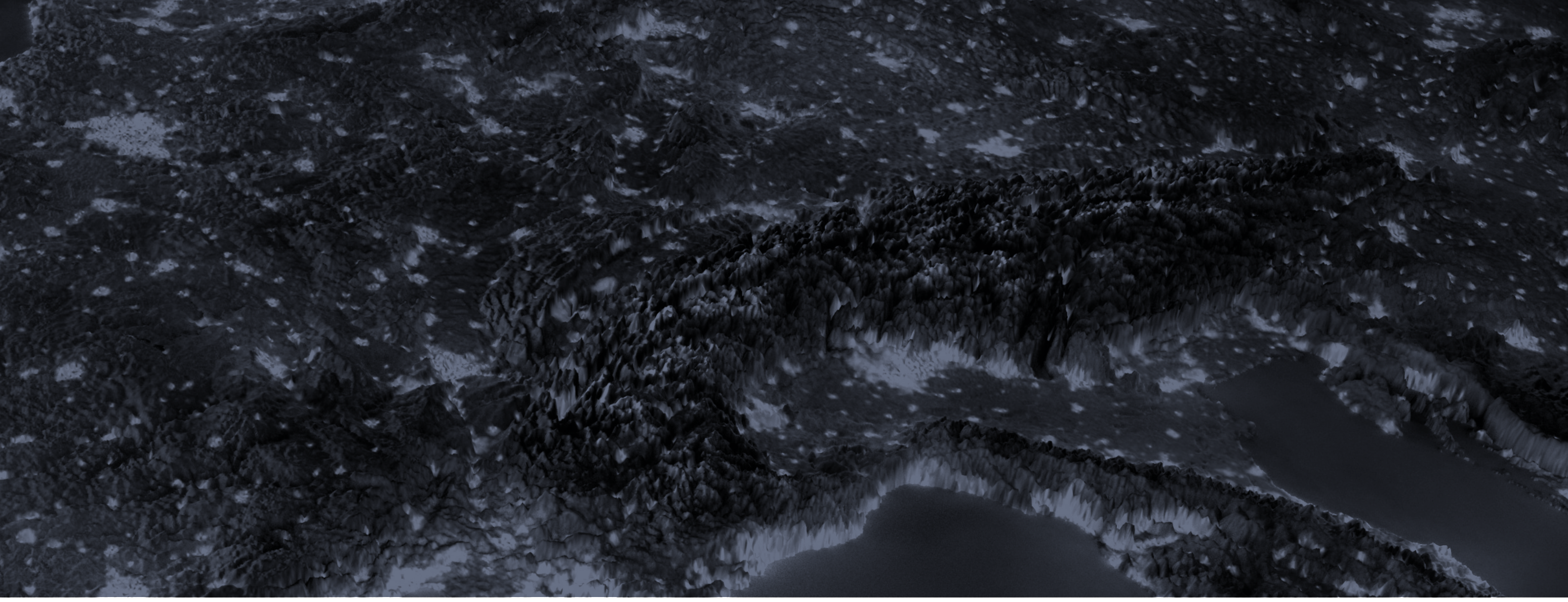
Cevian at ThyssenKrupp
Active Ownership Capital at PNE
Elliott Management at GEA Group

France

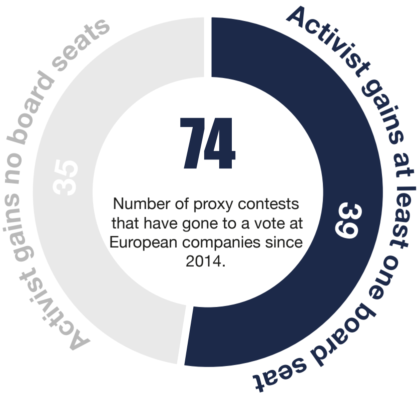
CIAM at Scor
Amber Capital at Lagardère
Sterling Strategic Value at Latécoère

Switzerland

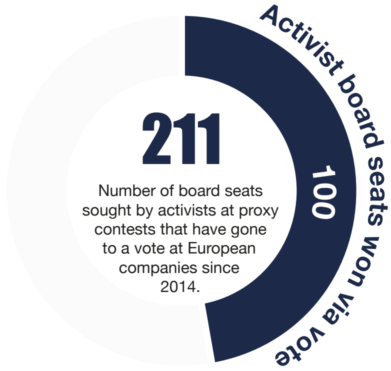
Third Point at Nestlé
Larius Capital at Aryzta
Q Investments at Weatherford International



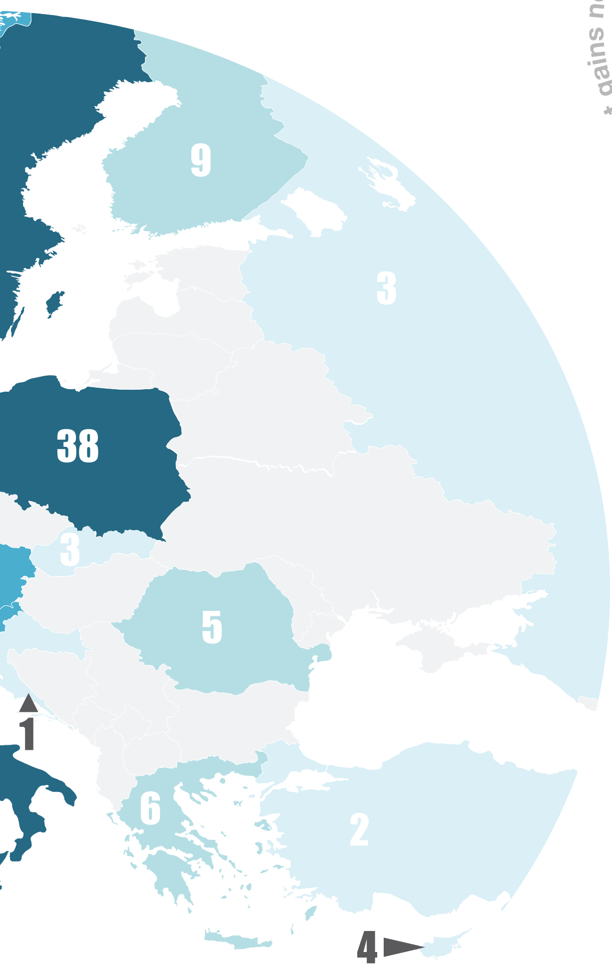
Proxy contest vote outcomes



Outcome of proxy contests that reached a shareholder vote at Europe-headquartered companies since 2014.

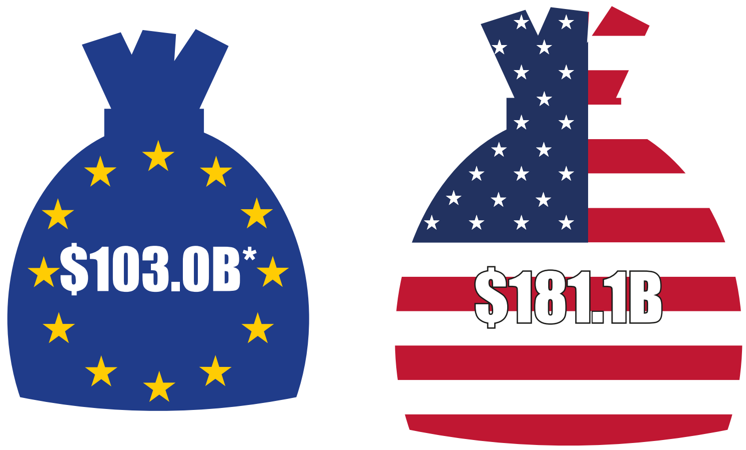


Number of board seats gained by activist nominees at proxy contests which reached a vote at Europe-headquartered companies since 2014.



Number of companies publicly subjected to activist demands by company HQ location between Jan 1, 2013, and Sep 30, 2018.

Activist capital invested in Europe and the U.S.



Value of newly disclosed activist investments at Europe- and U.S.-headquartered companies with a market cap over $200M disclosed between Jan 1, 2014, and Sep 30, 2018. (Values in US$)

*Includes Europe-headquartered countries that are not a member of the European Union.

A LEVEL PLAYING FIELD

David Rosewater, Managing Director, Global Head of Shareholder Activism and Corporate Defense and Jan Weber, Managing Director, EMEA at Morgan Stanley.

David, you had predicted a spike in European activism some time ago and it's now happening. Do you expect this trend to continue?

David Rosewater: Yes; if you look at the campaign activity over the last three years, it has grown at twice the rate of global activity, with the number of campaigns exceeding well over 100 each in all of the past three years. Another notable trend is that activist campaigns in Europe are focusing on larger companies with significant amounts of capital being deployed.

This trend is likely to continue because of valuations in Europe that are very attractive. Another factor is the homogenization of shareholder bases between the U.S. and the rest of the world, including Europe. This is very helpful to activists when running a campaign, because they end up interacting with large U.S. investors, whom they know well and have built relationships with over the years; in fact, these shareholders are accustomed to U.S.-style shareholder activism, and it is unlikely that they would approach these situations in a substantially different way based on geography, as they owe their investors the same fiduciary duties for all their investments.

Is it harder to be an activist in Europe?

Jan Weber: Although this answer can vary significantly based on what jurisdiction you are looking at, I would say that in many countries, the applicable rules are fairly friendly to activists and shareholders. Notwithstanding this favorable legal and regulatory framework, I believe that an activist's ability to be effective is somewhat limited by the less extensive history of big activist campaigns in those jurisdictions. A few large activist campaigns that go to a vote can certainly result in activism being more "mainstream."

Will activist success rates increase over time?

DR: I believe the success rate may have somewhat decreased in Europe as compared to a few years ago because the low hanging fruit has already been taken; however, in the longer run, we predict that success rates will continue to improve.

The increasingly homogeneous shareholder base across the U.S. and Europe is likely to create a similar playing field and to make more local European shareholders more receptive to activist views, assuming activists continue to be able to generate alpha. Absent a major regulatory/legal change, I expect it to be increasingly easy to launch a successful activist campaign in Europe as time goes by.

How influential do you think activists are when it comes to M&A and deal-making in Europe?

JW: Activists have been very focused on M&A on both sides of the Atlantic. With increased amounts of capital consistently going into passive strategies both in the U.S. and Europe, activists (together with some prominent active fund managers) are the shareholders that are most likely to be publicly vocal on these types of transactions.

How does a company increase its chances of success in an activist campaign?

DR: Knowing your shareholders well and having a good pulse on their level of dissatisfaction is key. That coupled with having a board that thinks about strategy carefully, articulates it clearly to the market in a way that allows shareholders to assess progress and challenges management appropriately on these themes and topics. Clearly, what makes for the best chance of success is also top-notch preparation, which includes picking the right advisers; you can very easily identify situations in which a company has done a lot of preparation work before a campaign becomes public and others where the company is playing "catch-up" once the campaign is public.

"The increasingly homogeneous shareholder base across the U.S. and Europe is likely to create a similar playing field."

-David Rosewater
david.rosewater@morganstanley.com

"Activists have been very focused on M&A on both sides of the Atlantic."

- Jan Weber
jan.weber@morganstanley.com

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Morgan Stanley is proud to be named the Leading Activist Defense Advisor for the second year in a row.[1] We serve our clients by helping them to achieve their strategic objectives through skilled execution, with innovative solutions suited to their specific circumstances in an ever-evolving and sometimes difficult market. This is done through close collaboration with colleagues across businesses and geographies to deliver the best of the firm to our clients. Morgan Stanley provides clients with advice relating to shareholder relations and corporate defense matters including dealing with activist shareholders or responding to unsolicited proposals and has the leading shareholder activism and corporate defense franchise. Our approach is grounded in the first-class service and high standard of excellence that have always defined the firm.

Learn more at **morganstanley.com**

[1] Source: Thompson Reuters

COUNTRY PROFILE
GERMANY

Iuri Struta, Activist Insight.

IN line with other continental European countries, activism in Germany has declined this year, with 11 companies targeted year-to-date compared with 17 during the same period last year and 16 in 2016. Absent a spike in activity in the next few months, 2018 will mark the slowest year since 2015.

Yet the media attention around the ThyssenKrupp drama involving two activists has more than offset the perception of declining overall activity, as the campaign is perhaps the biggest Continental bust-up in years. ThyssenKrupp is one of the last German conglomerates that has not yet restructured into a more focused entity, marking itself out as a target for activists.

Sweden-based Cevian Capital has been pushing ThyssenKrupp's management for years to reorganize its conglomerate structure by giving more independence to its four main business units. The emergence of Elliott Management as an investor in 2018 has increased pressure on the firm and led to the departure of both its chairman and CEO once a hotly contested merger of its steel unit with Tata Steel was revised. Although the powerful Krupp Family Foundation and employee representatives had come out against a separation, ThyssenKrupp announced a breakup to create two new entities focused on industrials and materials. Cevian welcomed the move, saying it was "an important step to tackle the underperformance of the past."

The campaign might prove crucial for the public's perception of activist investors, which have not been viewed in a positive light. "ThyssenKrupp is associated with good old Germany but at the same time many understand that it has a lot of issues. If a good solution is found, that could be a powerful signal in favor of activism," Till Hufnagel, a partner at activist fund Petrus Advisers, said in an interview for this report.

Further down market, finding easy targets has been difficult, in part because a stock market rally in 2017 led to lofty valuations. "Finding good value has been hard, valuations have been very, very high," Hufnagel reckons. Germany, long known as a fertile ground for bumpitrage plays due to its lavish protections for minority shareholders in deals, has had competition from more active M&A markets, leading to fewer opportunities for specialists such as Petrus.

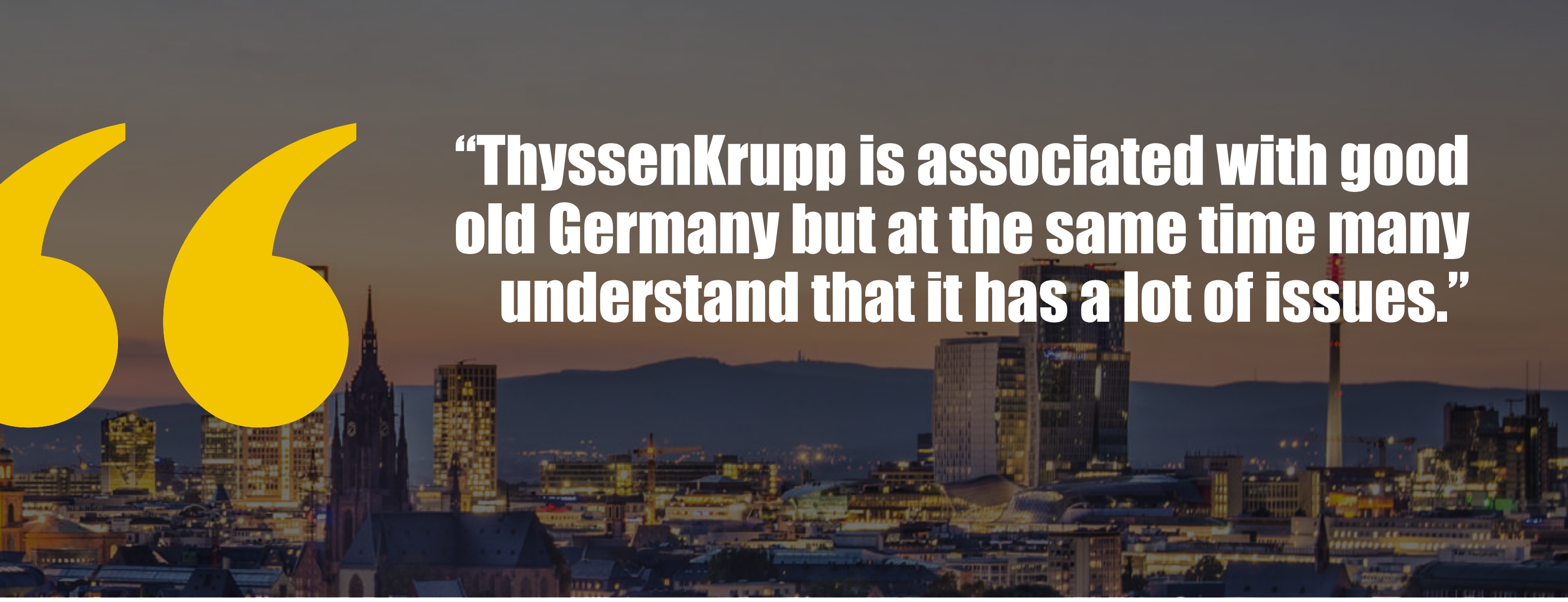
Yet the stock of utility company Uniper is trading at around 26 euros after Finland-based Fortum launched a takeover offer of 22 euros per share. The public opposition of Knight Vinke Asset Management and the involvement of Elliott increased bets that Fortum would have to compensate minority shareholders more richly after acquiring a 46% stake from E.ON.

The new reality has prompted Petrus to move further east, to Czechia. It launched two campaigns there this year: at Moneta Bank, where it backs management, and Unipetrol, where it launched a bumpitrage campaign with the use of appraisal rights to protect against a squeeze-out.

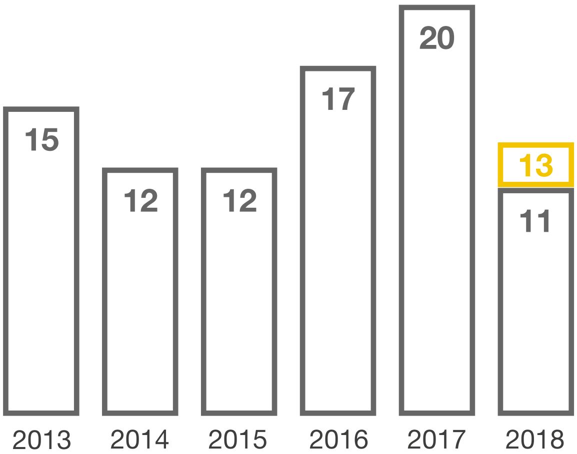
Meanwhile, Active Ownership Capital has focused on existing campaigns at PNE, a wind farm developer where it works with management on an expansion strategy, and Schaltbau. In addition to ThyssenKrupp and Uniper, Elliott targeted GEA Group, an equipment provider for the food industry, seeking margin improvements and the head of its chairman.

A more than 10% fall in the Dax index during the first half of 2018 might prompt activists to start hunting again. Hufnagel says Petrus' pipeline of upcoming situations is mostly in Germany and he feels that many other investors are looking at the country. "We see plenty of companies with improvement potential. The opportunities are there and should continue to grow," he said.

"We see an increased number of opportunities in the market, as valuation levels in Europe – and in particular in the German-speaking region – are reasonable as compared to more elevated levels in the U.S.," Klaus Roehrig, founding partner of Active Ownership Capital, said.

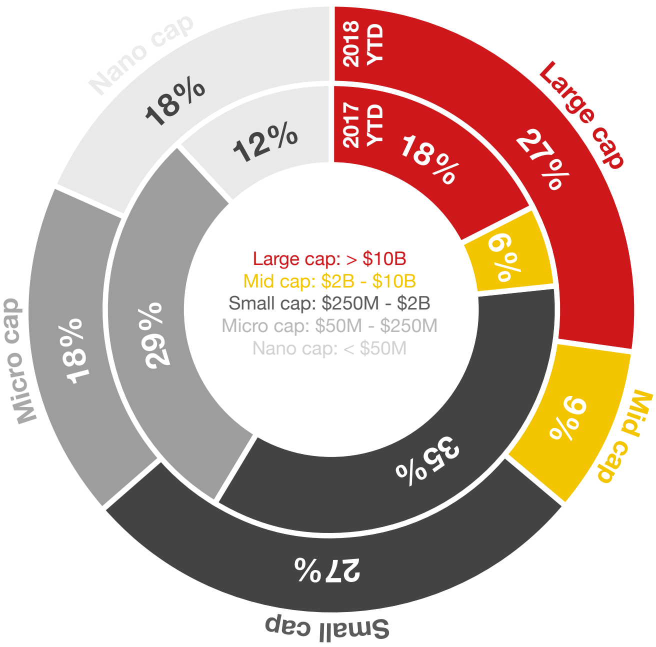


German targets by year



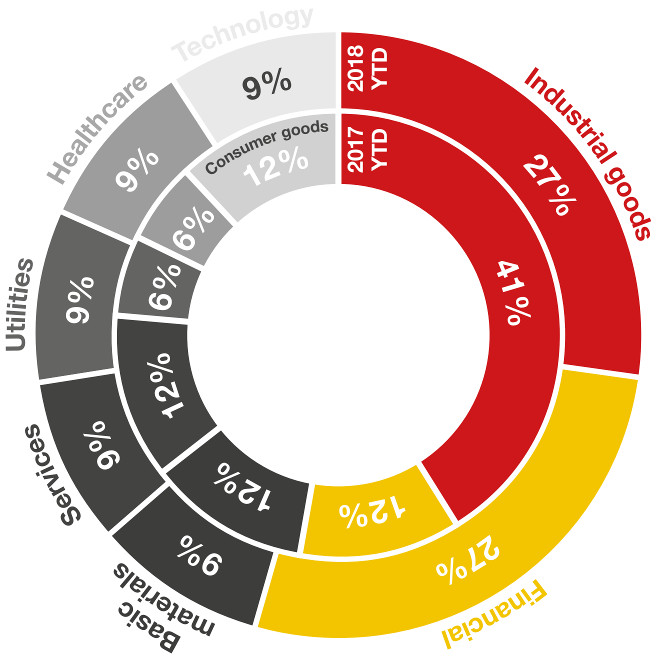
Number of Germany-based companies publicly subjected to activist demands. 2018 data as of Sep 30. Figure in yellow box is a projected 2018 full year figure.

German targets by market cap



Market cap breakdown of Germany-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

German targets by sector



Sector breakdown of Germany-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

59%
Proportion of resolved public activist demands at Germany-based companies at least partially satisfied.

30
Number of board seats gained by activist nominees at Germany-based companies since 2014.

6
Number of Germany-based companies publicly subjected to **Elliott Management's** activist demands since 2013.

LEGAL ANALYSIS
GERMANY

Matthias Horbach and Holger Hofmeister, Skadden.

IN 2018, shareholder activism continued to be a driver for change to the corporate landscape in Germany, launching or bringing to an end some noteworthy public campaigns (such as ThyssenKrupp, Deutsche Bank, and Volkswagen) and has led to an increase of the M&A volume in Germany. Whilst overall activity to the extent publicly relevant rises continuously, the numbers relative to the size of the economy and of the capital markets remain low.

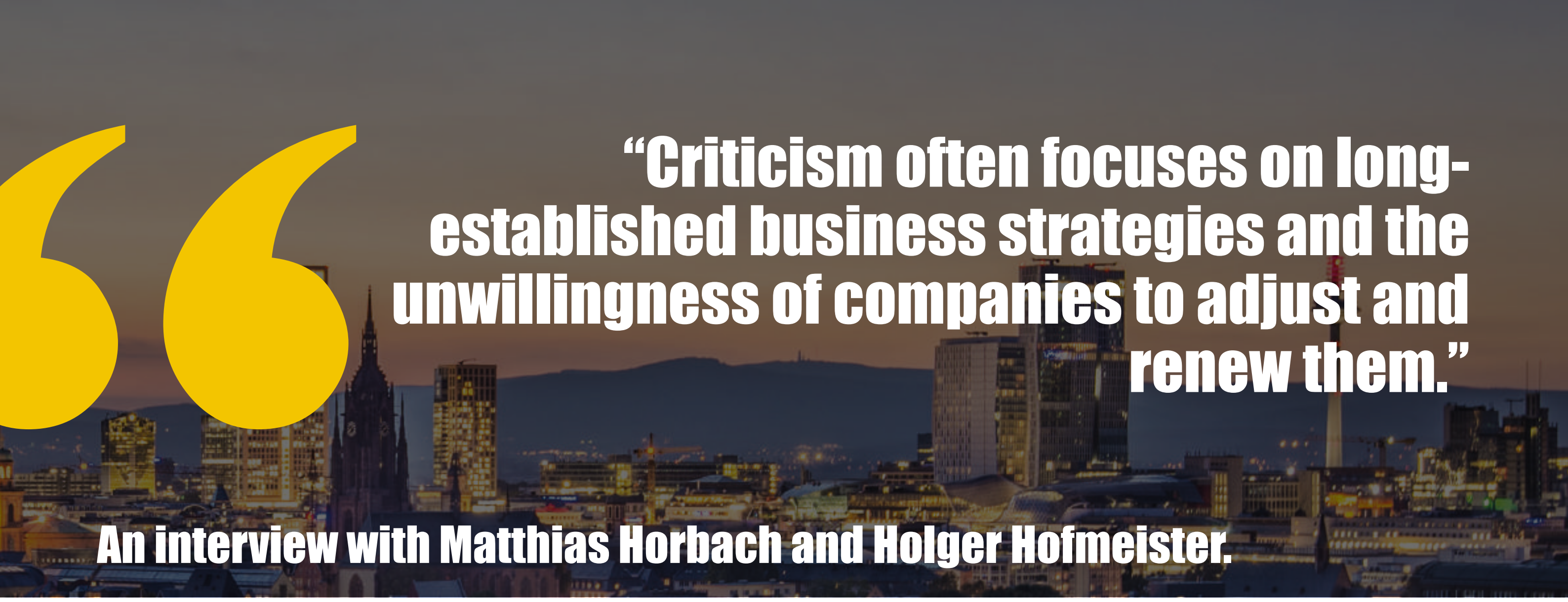
The results are in: Active Ownership Capital's (AOC) campaign targeted at German pharmaceutical company Stada and initiated in 2016 has been among the most prominent cases in Germany. This campaign resulted in a shake-up of the company's management and supervisory board (the CEO and the chief financial officer left the company) and Bain Capital and Cinven acquiring a 64.5% stake in Stada. However, the implementation of a control and profit transfer agreement required a 75% majority of votes present. For their consent, Elliott, holding 15.2% including options, demanded an increase of the compensation to 74.40 euros per share in cash. Bain Capital and Cinven accepted such increase, i.e. 8.9% above the takeover price of 66.25 euros.

Elsewhere, a Cevian Capital and Elliott campaign targeted ThyssenKrupp's planned joint venture combining its European steel unit with Tata Steel, leading to the resignation of both management and supervisory board chairs. Cevian and Elliott desired to stop the joint venture in order to realign and refocus the divisions of ThyssenKrupp more efficiently as well as to see changes to the management board. These investor initiatives were supported by representatives of other shareholders, including the chairwoman of the Alfried Krupp von Bohlen and Halbach Foundation. In this context, ThyssenKrupp interim CEO Guido Kerkhoff also expressed his goal for more segmentation and active portfolio management, holding that there was no clear evidence that two or three companies could not work under the same roof.

Elliott is also still busy with its investment in GEA Group, a provider of industrial automation and industrial products and services. After having requested a substantial share-buyback, Elliott is now calling for a strategic review to enhance stakeholder value. In addition, Elliott is urging the company to appoint a new CEO without further delay as well as to strengthen the composition of the supervisory board, including the replacement of the current chairman.

Activists' demands are evolving: Over the last year, shareholder activism did not only focus on "typical" goals such as obtaining board seats or urging companies into M&A transactions. It also comprised demands to change the business, such as active portfolio management, especially of conglomerates, and catalyzing and communicating the dissatisfaction of shareholders. For example, Petrus Advisers pressured Commerzbank as majority shareholder of comdirect to treat minority shareholders more fairly. Deutsche Bank hired a unit of Cerberus Capital Management to advise the lender on how to hit the planned profit targets by driving down costs and squeezing extra revenue. After Elliott had called for a special audit to investigate potential violations of law by Uniper's management during the Fortum takeover bid, the annual shareholder meeting of Uniper decided to appoint a special auditor to identify any such breaches.

Taking into account the growing number of educated investors who are willing to actively engage in discussions with boards, and ongoing, often technology-driven changes and challenges to various business sectors, shareholder activism will likely be developing and playing an even more important role in Germany over the next few years.



"Criticism often focuses on long-established business strategies and the unwillingness of companies to adjust and renew them."

An interview with Matthias Horbach and Holger Hofmeister.

Is the level of activism in the public eye indicative of the volume of activism behind-the-scenes?

No. The level of activism in the public eye is mainly driven by the impulse-giving large hedge funds that target well-known corporations whose stock is publicly traded on a recognized stock exchanges. While the number of reports on visible activism campaigns has increased, activism behind-the-scenes continues to be the preferred approach by a number of activist shareholders, and even for those that are prepared to pursue their goals publicly an approach behind-the-scenes is often the start of a campaign.

Are German two-tier boards no longer a defense against activism?

Two-tier boards continue to be a defense against activism. Shareholders have only indirect influence over the management board. They are in large part limited to expressing their discontent publicly or in shareholder meetings, and to passing a no-confidence vote on individual members of the management board. It is the supervisory board that can, and should, identify certain actions within the scope of responsibility of the management board that require its prior consent.

Will activists continue to demand special auditors in M&A deals?

Yes, we expect that activists will continue to demand the appointment of special auditors in M&A deals. As recently seen in the takeover bid by Fortum for Uniper, the appointment of a special auditor and its report can create significant pressure on the parties of a takeover bid. Special auditors are to be appointed upon shareholder resolution or upon demand of minority shareholders holding a certain minimum number of shares. The demands for the appointment of auditors extend to the review of, inter alia, business relationships with affiliates, other parts of the management of the corporation, and certain capital measures. The combination of minority shareholder rights and the requirement to publish the report enables activist shareholders to exert pressure on boards to take certain actions or implement specified plans.

How is the Shareholder Rights Directive affecting corporate governance in the country?

The rules on "say on pay," when implemented, will establish rights for shareholders to vote on the consideration payable to management board members. The national legislator can decide whether the vote is binding on the corporation or constitutes only a recommendation. If the shareholder vote is binding, the competency to determine the consideration of members of the management board will effectively shift from the supervisory board to the shareholder meeting. If the shareholder vote provides a recommendation only, the supervisory board would retain a level of responsibility. It would retain actual decision power but is expected to take the shareholder vote into account.

The provisions of the directive on related-party transactions do not specify which body (shareholders meeting or supervisory board) shall be competent to approve related-party transactions. If such approval rights end up with the supervisory board, minority shareholders will not be able to participate in such decisions and their rights to challenge decisions will be limited.

Why is operational activism seemingly on the rise in Germany?

Criticism often focuses on long-established business strategies and the unwillingness of companies to adjust and renew them. In addition to divestitures, activists therefore frequently demand, for instance, the reorganization of activities that do not have significant interrelations in divisions with the goal of creating higher specialization. A number of corporations such as Daimler, Continental and ThyssenKrupp have established, or are currently establishing, holding company structures. The resulting divisions cannot only be operated separately and, arguably, more effectively, but can also be sold, listed separately or managed with third-party investors or joint venture partners. However, as many corporations retain their existing strategies, the number of potential targets for operational activism remains high.

COUNTRY PROFILE
ITALY

Iuri Struta, Activist Insight.

THE battle between French corporation Vivendi and the London branch of U.S. hedge fund Elliott Management over Telecom Italia was a banner moment for activism in the country. Irrespective of whether the campaign will lead to higher activity levels in the years to come, the situation showed Elliott can team up with governments, as well as fight them.

Elliott successfully installed fresh directors representing a majority of the TIM board in May, beating Vivendi's alternative slate. The alienated Italian government, which had been displeased with the control exercised by Vivendi over assets it deems of strategic importance, bought a stake in TIM and tacitly supported Elliott's slate. Despite low support in Italy, Vivendi is not backing down. It has attacked the performance of TIM several times since Elliott won the proxy contest and has been working on mending fences with the Italian authorities.

The amount of attention the TIM campaign generated has concealed rather subdued activity levels. At the end of September, seven companies have been targeted by activists in 2018, down from nine in the same period last year and 12 in 2016.

In the shadows of the TIM campaign, Retelit, another telecom firm which owns 12,500 km of fiber-optic cables, has been dealing with drama of its own. A group led by Shareholder Value Management won control of the board against an alternative slate advanced by an Italian investor. But the government exercised its golden power over Retelit's assets of national interest, because Shareholder Value failed to notify it of an accord inked with Libyan investor Bousval and German fund Axxion over their collective 24% shareholding.

In addition to buoyant activity in the telecom sector, another noticeable trend is the increased interest in Italy's embattled banking sector. Plagued by high levels of bad loans and needing capital injections as their balance sheet cleanup enters their final innings, Italian banks have low valuations and continued to attract investors of all sorts.

Amber Capital, an activist focused on the Southern European region, is campaigning for Banca Popolare di Sondrio to convert itself from a cooperative bank (one shareholder - one vote) to a joint stock company (one share – one vote) in order to attract foreign capital further down the road.

As banks' shareholder structures change following equity raises, the urgency for action increases. After building a 5.8% stake in a 700 million euro equity issuance, Denis Dumont successfully launched an initiative to overhaul the board of Sondrio-based Credito Valtellinese. Banca Carige saw two factions of shareholders battling for control amid calls from the European Central Bank to resolve its governance crisis and capital requirements via a merger. Malacalza Investimenti marginally won the battle against another large shareholder, Raffaele Mincione.

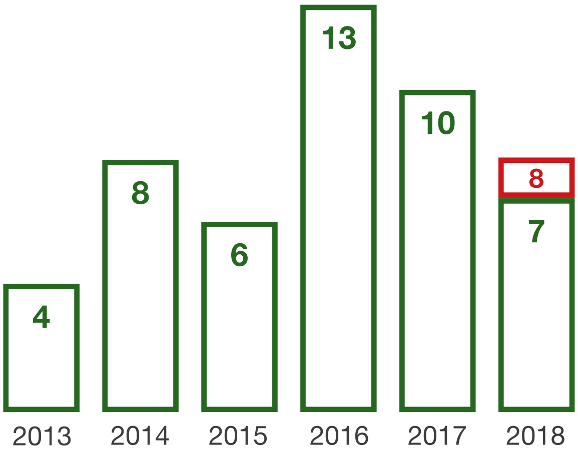
Yet bigger undertakings may lie ahead as a sector consolidation gathers pace, in part due to pressure from the Bank of Italy. "The ownership structure of several Italian banks is fragmented and there is the possibility for activist investors to play an important role in asking managements to implement value-constructive initiatives," Arturo Albano, head of corporate governance at Amber, said in an interview for this report.

"The banking sector has been very active, although for the wrong reasons," notes Marco Taricco, founding partner of Bluebell Partners, an adviser to activists, citing non-performing loans and examples of mismanagement. "This evidently creates opportunities for investors. There has been some consolidation, but there is a need for more."

A big uncertainty for investors is the anti-establishment Italian government. The Retelit case is an indication that the new authorities will keep a close eye on deals and intervene more often, particularly in sectors of national interest.

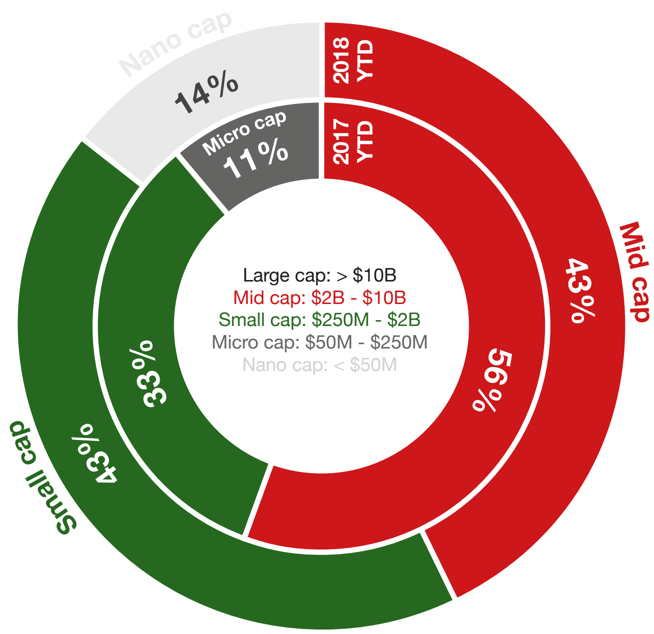
> "The banking sector has been very active, although for the wrong reasons."

Italian targets by year



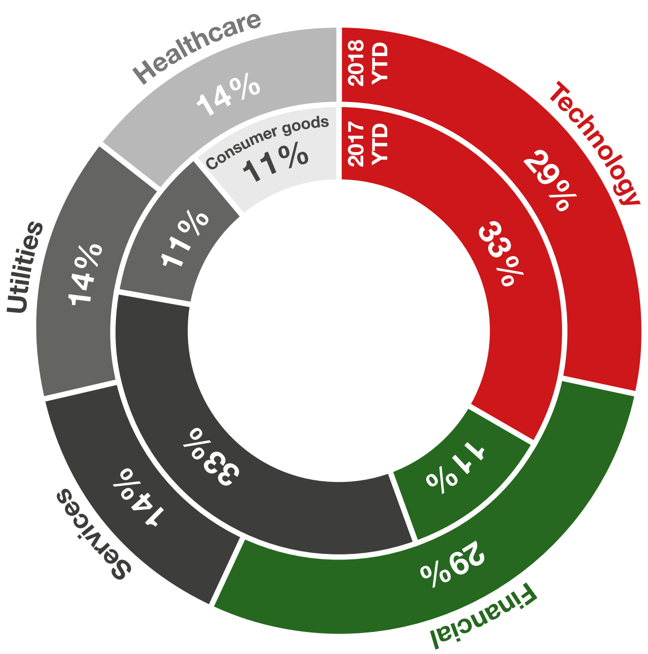
Number of Italy-based companies publicly subjected to activist demands. 2018 data as of Sep 30. Figure in red box is a projected 2018 full year figure.

Italian targets by market cap



Market cap breakdown of Italy-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.

Italian targets by sector



Sector breakdown of Italy-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

72%

Proportion of resolved public activist demands at Italy-based companies at least partially satisfied.

107

Number of board seats gained by activist nominees at Italy-based companies since 2014.

22

Number of Italy-based companies publicly subjected to **Amber Capital's** activist demands since 2013.

LEGAL ANALYSIS ITALY

Lorenzo Corte, Skadden.

IN the last three years, Italy has registered more public activist campaigns than several other European countries with larger and more mature capital markets. What is striking is not only the level of activity, but the intensity of the campaigns run by activists and the targets, which include companies once thought to be untouchable and protected by the Italian establishment or government.

In the very public instance of Telecom Italia, activist investing becoming more creative and sophisticated in the face of a traditional, insular, and resistant Italian corporate culture was on clear display. Decreasing ownership of companies and publicly listed shares by traditional Italian institutions and the parallel adoption of regulations to increase transparency in the capital markets and guarantee a seat at the table for minority shareholders has given the activists the toolbox they needed to implement effective campaigns. The board reshuffle following the proxy contest at Telecom Italia indicates that board seats can be won when an actor is willing to push a contest all the way to a shareholder vote.

Other investors, such as London-based Amber Capital, are also operating independently and alongside Elliott, including in an ongoing set of legal disputes regarding corporate management and oversight at Italian manufacturer Ansaldo. Collectively, these activities again illustrate the diversity of industries targeted by activist investors in Italy, but they also underline the diversity of strategies deployed by activist investors, as well as their assertiveness and increasing confidence operating in the Italian context. Unsurprisingly, this range of targets and activities highlights the vigorous activity of foreign funds in Italy over several years, indicating that the role of activism in Italian markets is unlikely to retreat and has become a permanent fixture.

Demonstrating that untouchables no longer exist in Italy, London-based distressed credit fund Caius Capital initiated a letter campaign to convince shareholders at UniCredit to demand that 3 billion euros of complex instruments be converted to common equity. Caius also submitted a letter to the European Banking Authority demanding an investigation into the UniCredit issuance of, and regulatory oversight of, securities in 2008, indicating that the trauma of the 2008-2009 recession has yet to fully work its way through the Italian financial system and continues to catalyze promising targets for activist investors. Particularly in light of the diverging economic performance of economies both within and outside Europe such suspect performance is likely to continue to generate investor interest in vulnerable Italian targets.

Additionally, although most analysis tends to focus on the targeting of Italian business interests by foreign activist investors, less attention has been paid to the reverse phenomenon. Following a July 2018 proposed options offering to directors to incentivize performance and retention, Italian businessman and CEO of Algebris Investments Davide Serra mounted an attempt to replace the CEO and board chair of London-listed Telit Communications. This activism has yet to be resolved but does indicate that as the Italian corporate community becomes more exposed to investor activism, it is increasingly likely that Italian actors will seek to engage in similar opportunities outside the domestic context.

As a conceptual lesson, the role of corporate governance and culture in Italy is more nuanced than is always appreciated, for instance, as a window into the voting behavior of investors, in part because shareholder votes in Italy are part of the public record. Because of the important role of traditional institutional investors such as Vanguard and BlackRock, such as in the ultimate board alignment between Elliott and Vivendi at Telecom Italia, and the unprecedented role of the Italian state in supporting the corporate vision of a foreign activist investor, the varied actions of investor types is on unusually transparent display.

Collectively, these issues of board composition struggles, sector-wide malaise, and nuanced domestic corporate cultures mean that Italy continues to be an evolving investment environment. It displays a mix of domestic, European, and international tensions and trends that indicate investor activism is likely to continue and will generate diverse opportunities in the changing landscape.

“Board composition struggles, sector-wide malaise, and nuanced domestic corporate cultures mean that Italy continues to be an evolving investment environment.”

An interview with Lorenzo Corte.

Is the level of activism in the public eye indicative of the volume of activism behind-the-scenes?

The current investment climate in Italy is one of consistently high activity. This is a continuation of the trend that emerged following the recession, when disruption of the local market created new investment opportunities that constitute the fertile ground now surveyed by investors. Though speculation on behind-the-scenes investment must necessarily derive from anecdote and analysis of market fundamentals, even more investment outside of public view must be occurring.

How is the Shareholder Rights Directive effecting corporate governance in the country?

The Shareholder Rights Directive influences Italian corporate governance through its various requirements that companies both identify and communicate effectively with shareholders, as well as endeavor to facilitate their participation in corporate decision-making. This European-level mandate runs parallel to the more decisive domestic Italian regulations that also serve powerfully to facilitate activist investor operations. For instance, shareholders owning 2.5% of shares can call a special meeting, while shareholders holding 0.5-4.5% (depending on market cap) of shares are entitled to submit slates of nominees to the boards of directors or of statutory auditors.

In this market environment, on a preemptive level, companies will continue to allocate resources to increasingly robust investor relations, particularly through independent directors, with an eye to cultivating a more fine-tuned understanding of the investment conditions in which they operate. On a reactive level, companies are likely to ensure that their internal capacity and planned responsiveness to investor activism are primed and competent to respond effectively.

How seminal will the Telecom Italia proxy fight prove to be?

The Telecom Italia proxy fight will prove seminal as the most dramatic illustration of the current overall prominence of investor activism internationally and its expression in Italy specifically. The convergence of several forces, including the domestic financial sector pressures unresolved in Italy from the recession, the increasing assertiveness of foreign and particularly non-European activists, and the unprecedented role of the Italian state in choosing to align its shareholder interest with activist investors in the form of Elliott, alongside the relative isolation and unpreparedness of the Italian corporate actors, all combined to create a unique and perhaps irreplicable illustration of the current market disruption unfolding in Italy.

Holdouts in M&A continue to be a problem for Italian companies. How can deals avoid this fate?

The role of holdouts in the context of M&A activity in Italy continues to be dominated by the decision of Italian policymakers to maintain the requirement that 95% of shareholders accept takeover offers to enable squeeze-outs of minorities. This high threshold necessarily blunts the effectiveness of potential investors in the face of recalcitrant minority stakeholders. Holdouts will continue to affect the M&A environment in Italy as long as this structural barrier persists.

EU regulation does permit a level of national discretion in setting the threshold barrier to minority protection to a lower threshold (90%), which other countries have moved to in the years following the implementation and testing of the takeover directive. As such, the role and power of holdouts remains primarily a policy question, rather than one of deal construction or preparation in the private sphere.

COUNTRY PROFILE
SWITZERLAND

Iuri Struta, Activist Insight.

ACTIVISM has been a rare occurrence in Switzerland this year, as a stock market rally in the second half of 2017 may have prompted activists to stay on the sidelines. Just six Swiss companies have been targeted so far in 2018, representing a four-year low. During the same period last year, eight companies were targeted, extending to nine for the full year.

Most notably, Third Point Partners reignited a campaign at food and drink giant Nestlé in July, calling for a "bolder" overhaul of its portfolio of products and simplification of its "overly complex organizational structure." In typical U.S. style, Third Point launched a website and a presentation advancing its case but has yet to take further steps, leaving many to wonder whether it will bother with a proxy contest.

In November 2017, Credit Suisse found itself in the crosshairs of local activist RBR Capital, which asked for a three-way breakup. The company met with the activist, and Harris Associates, a large anchor shareholder, said part of RBR's thesis had merits after initially dismissing the idea.

There are signs activism could mount a return, however. After peaking in January, the Swiss stock market has been falling, with Credit Suisse prominent among the underperformers. Rick Hochfeld and Gregor Joos, former partners at RBR, have launched a new activist fund, named Larius Capital, to focus on the small- and mid-cap arena.

Hochfeld sees many investors stuck in "value traps" that could be unlocked via activism and has already identified a number of potential targets. In September, Larius targeted Zurich-based Aryzta, a specialty baker, seeking to block an 800 million euro capital raise and instead cut costs and sell non-core assets. Cobas Asset Management, a large shareholder, joined Larius in its call against the capital increase and advanced an alternative plan. Proxy adviser Institutional Shareholder Services also opposed Aryzta's scheme.

Because the market is still underpenetrated, Hochfeld believes an activist strategy could be very "lucrative," particularly given the favorable shareholder rights compared with other regions in continental Europe.

Ali Saribas, a partner at shareholder advisory firm SquareWell Partners, sees higher potential with mid-cap firms because "there are more companies with a shareholder structure that provides more opportunity for activists to convince as opposed to the mega, small, and micro caps."

The perennial issue of reference shareholders is particularly pertinent in the small-cap segment of the market. According to Saribas, more than half the 200 companies listed in Switzerland have an anchor shareholder which owns at least a third of the shares. An average turnout rate of around 70% at annual meetings makes it even harder for an activist to move against management.

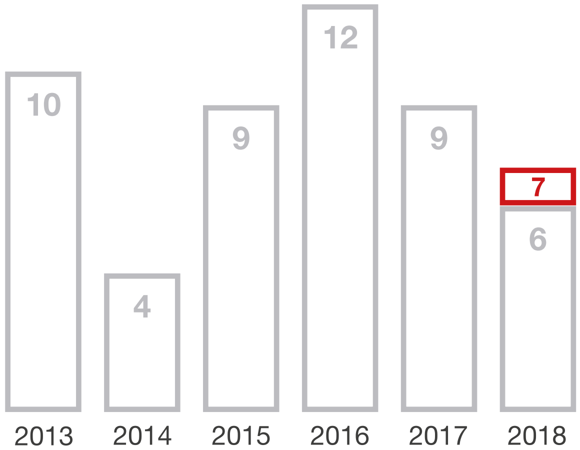
Yet Hochfeld is optimistic that an anchor investor will not necessarily back the status quo if leadership underperforms. "If an anchor shareholder lets management and the board destroy shareholder value and remains confident that the same guys will be able to turn everything around, then the impact of an activist will be very limited," Hochfeld said.

An area of focus for activists will continue to be capital allocation and divestment of non-core assets, Saribas reckons. Meanwhile, the growing importance of good governance practices, including environmental, social and governance issues, may be a way for activists to win the hearts of institutional shareholders.

"Except for a few Swiss companies, shareholder engagement on extra-financial issues is still not carried out which may position them as entrenched boards," Saribas said. "We feel that with the new regulations being considered by the Swiss Parliament to have companies conduct mandatory due diligence on human rights and the environment may push companies to engage more with their investors on such issues."

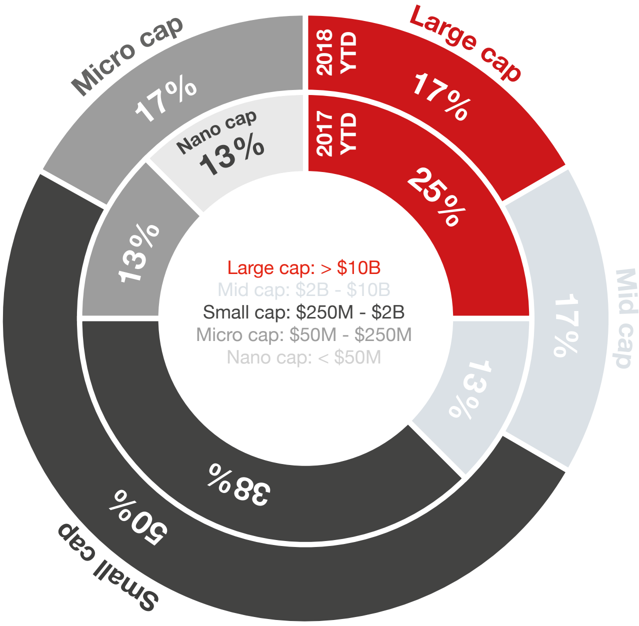
> **"Shareholder engagement on extra-financial issues is still not carried out which may position them as entrenched boards."**

Swiss targets by year



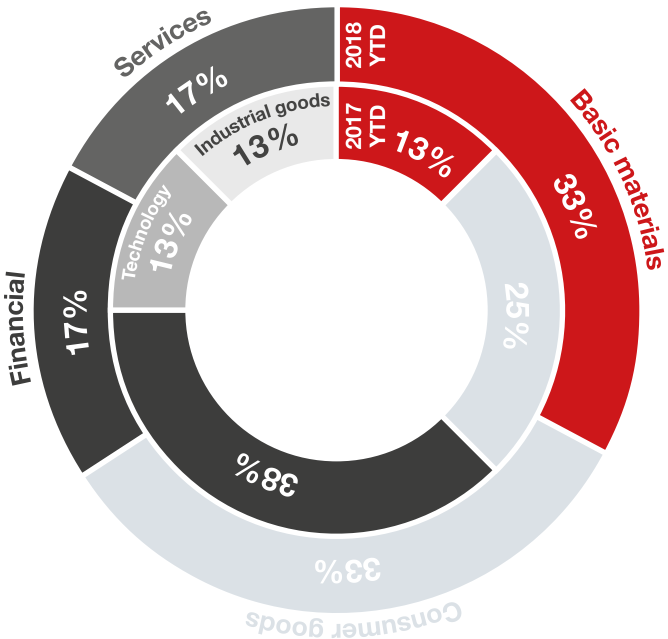
Number of Switzerland-based companies publicly subjected to activist demands. 2018 data as of Sep 30. Figure in red box is a projected 2018 full year figure.

Swiss targets by market cap



Market cap breakdown of Switzerland-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

Swiss targets by sector



Sector breakdown of Switzerland-based companies publicly subjected to activist demands between Jan 1, 2017, and Sep 30, 2017, and Jan 1, 2018, and Sep 30, 2018.
Note: Rounding may lead to summation errors.

38%

Proportion of resolved public activist demands at Switzerland-based companies at least partially satisfied.

15

Number of board seats gained by activist nominees at Switzerland-based companies since 2013.

5

Number of Switzerland-based companies publicly subjected to **Veraison Capital's** activist demands since 2013.

LEGAL ANALYSIS

SWITZERLAND

Mariel Hoch and Fabienne Perlini-Frehner, Bär & Karrer.

THE primary sources of laws and regulations relating to shareholder activism are the Swiss Code of Obligations (CO) governing the rights and obligations of companies' boards of directors and shareholders in general and the Swiss Financial Market Infrastructure Act (FMIA), enacted on January 1, 2016, containing additional rules for listed companies and their shareholders. The provisions of the FMIA are set out in more detail in two ordinances, the Swiss Financial Market Infrastructure Ordinance (FMIO) and the Swiss Financial Market Infrastructure Ordinance by FINMA (FMIO-FINMA).

Further, the Ordinance Against Excessive Compensation in Listed Companies (OAEC) contains specific rules on the compensation of management and boards of directors. The Takeover Ordinance (TOO) sets out detailed rules on public takeover offers including boards' and qualified shareholders' obligations. Companies listed on the SIX Swiss Exchange are also bound by, inter alia, the Listing Rules (LR-SIX), the Directive on Ad Hoc Publicity (DAH) and the Directive on Information Relating to Corporate Governance (DCG).

The CO and FMIA are enacted by the national parliament, the FMIO and the OAEC by the Swiss Federal Council, the FMIO-FINMA by the Swiss Financial Market Supervisory Authority FINMA (FINMA), the TOO by the Swiss Takeover Board and the LR-SIX as well as the DAH by SIX Exchange Regulation.

Compliance with the CO and the OAEC is primarily enforced by the civil courts. FINMA enforces the FMIA as well as its ordinances and the Takeover Board enforces the TOO and the takeover related provisions of FMIO-FINMA. Compliance with the LR-SIX, DAH and DCG is enforced by the SIX Exchange Regulation.

According to the CO, any shareholder – individually or acting in concert – representing 10% of the share capital or, according to the predominant legal doctrine, representing shares of a par value of at least 1 million Swiss francs, has the right to call an extraordinary shareholders' meeting. Certain companies have introduced lower thresholds in their articles of association. The request to call an extraordinary shareholders' meeting must be submitted in writing to the company's board and must contain the requested agenda items including the activist's motions.

Shareholders may not act by written consent in lieu of a meeting, but they can be represented by issuing written voting instructions to either the independent proxy or (depending on the articles of association) to another shareholder or a third party, including advisory firms. Prominent Swiss proxy advisers, such as Ethos, SWIPRA and zRating, publish general proxy voting guidelines, corporate governance principles as well as company-specific voting recommendations.

In case advisory firms do not receive specific voting instructions, such firms will generally exercise votes obtained according to the respective voting recommendation. Also, proxy guidelines issued by internationally known proxy advisers such as Institutional Shareholder Services (ISS) or Glass Lewis have developed considerable influence on the voting behavior at Swiss-listed companies' shareholder meetings.

According to the OAEC enacted on January 1, 2014, Swiss pension funds are obliged to exercise their voting rights related to their participation in listed companies with respect to certain agenda items (e.g., election of the board of directors and its chairman as well as the total compensation of the directors and the management). Since the exercise of the voting rights must happen in the best interest of the insured persons (and such interest is deemed preserved if the voting behavior is in furtherance of the continuing prosperity of the pension fund), pension funds tend to rely on the recommendations of the proxy advisers both for efficiency and potential liability reasons.

> **“When operating in the financial sector, activists typically take a more conservative approach in order to prevent damaging the reputation of the institution.”**

An interview with Mariel Hoch and Fabienne Perlini-Frehner.

Is the level of activism in the public eye indicative of the volume of activism behind-the-scenes?

In our experience, roughly half of all activist campaigns never become public – so the answer is no. This is because initially, activists will typically make private contact with the company’s executive management or board representatives in order to present and discuss their ideas and specific demands. Only if the private negotiations fail, activists may move to a launch of a public campaign to divulge their requests towards the company and by doing so seek the support of other shareholders and other financial markets stakeholders.

Activism in the banking sector has had limited impact in Switzerland despite high-profile situations. Is this because of the regulatory regime or the shareholder culture?

It is in our view rather the second. A further reason is that in the situations of UBS and Credit Suisse the activists held (or hold) very small positions (RBR Capital’s campaign at Credit Suisse is, however, ongoing). Another reason is that when operating in the financial sector, activists typically take a more conservative approach in order to prevent damaging the reputation of the institution which is one of its key assets. Consequently, there is also much less visibility as to the impact activists have in the financial sector.

What advantages or disadvantages do activists face in proxy fights at Swiss companies?

In Switzerland, all shareholders have the right to attend shareholders’ meetings, the right to vote and to request information and inspect certain documents (to the extent company interests requiring confidentiality do not prevail). The right to information is regularly used by activist shareholders to increase pressure prior to shareholders’ meetings. The board is obliged to respond to such questions during the shareholders’ meeting. All shareholders have the right to propose motions and counter-motions at shareholders’ meetings.

Furthermore, any shareholder representing shares of a par value of at least 1 million Swiss francs is entitled to demand that certain agenda items be tabled at the next shareholders’ meeting. Any shareholder representing 10% of the share capital may request that an extraordinary shareholders’ meeting be convened. According to the predominant legal doctrine, these thresholds should be regarded as alternative criteria.

Since it is outside the EU, is the Shareholder Rights Directive exerting any indirect influence on corporate governance in Switzerland?

Already in 2013, Switzerland adopted the Ordinance Against Excessive Compensation in Listed Companies (OAEC), which contains specific rules on the compensation of the members of the management and the board of directors and which is one of the principal points of improvement of the SRD. In addition, a guideline for institutional investors on the exercise of their participation rights in public limited companies was published in 2013 by representatives of the Swiss economy, institutional investors and proxy advisers. Strengthening the rights and responsibilities of shareholders and improving transparency in the area of corporate governance are also regulatory objectives in Switzerland.

How did the experience of Clariant, fending off activists and a hostile bidder, influence defense strategies in Switzerland?

There are a number of recent high-profile cases which have influenced defense in Switzerland. Besides Clariant, Nestlé and Aryzta have certainly provided good learnings. It has become clear that activists are sophisticated actors with the ability to point to weaknesses of their targets in a convincing manner. They often retain reputed external advisers to add credibility to their requests. A standard part of any defense rule book must therefore be to entertain an active dialogue with activist shareholders – but to do so privately, and to stay out of a public debate with them.

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2018