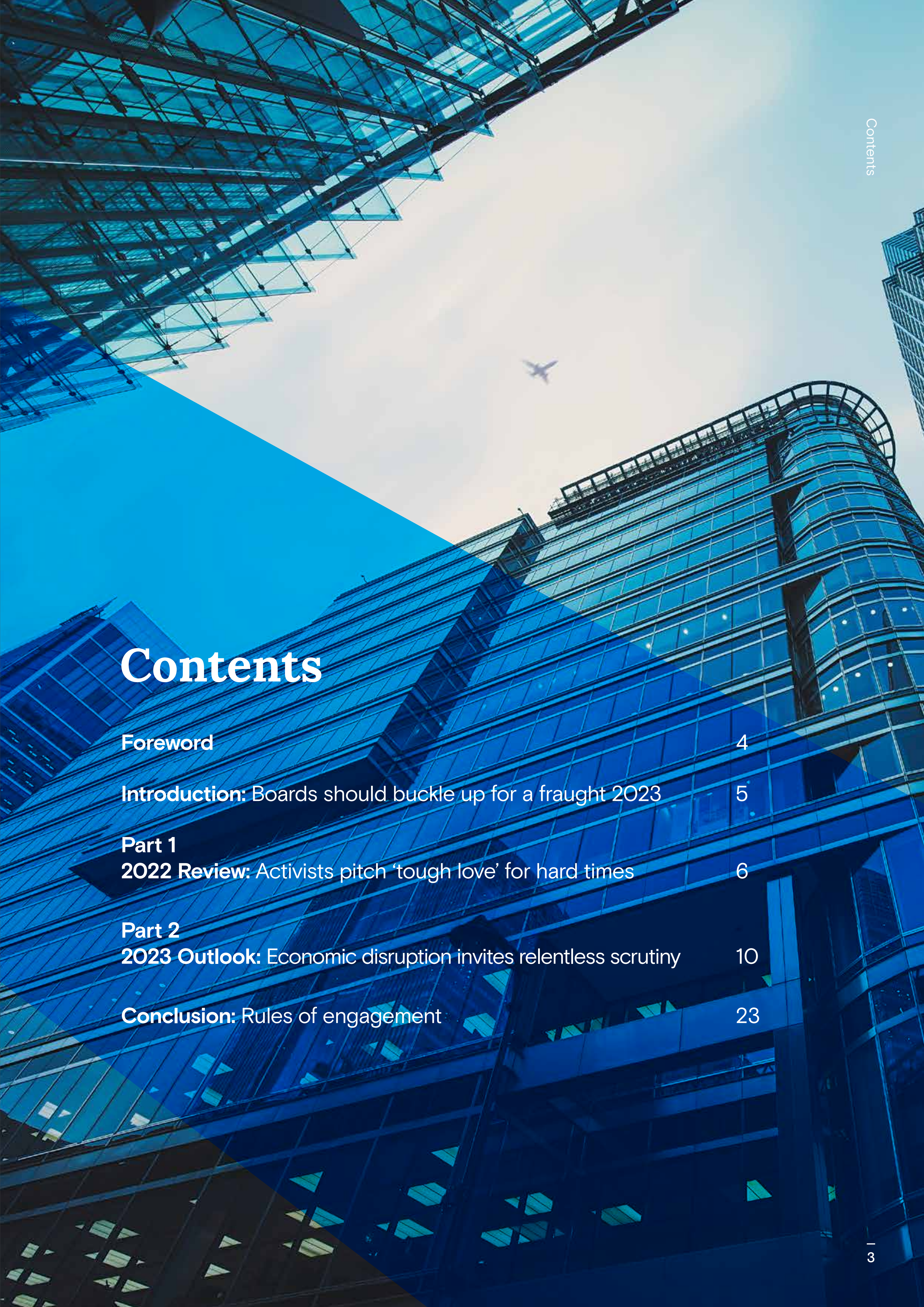
Activist Investing in Europe

2023

Activistmonitor

Skadden



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Foreword

Be ready and prepared – more than ever

Armand Grumberg
Head of Skadden's European M&A practice

In the face of major headwinds, the past year has shown that shareholder activism is very resilient. While shareholder activism 'defeated' the Covid-19 crisis and its consequences for the economy in 2020 and 2021, new challenges surfaced in 2022: the war in Ukraine, the return of inflation, and an energy crisis in Europe. Once again, shareholder activism has demonstrated its agility and ability to opportunistically adapt to every situation by reinventing its approaches and techniques.

The growing public concern for environmental, social & governance (ESG) issues, particularly in relation to Europe's ongoing energy crisis, has allowed the topic to mature quickly in activist circles. There is no doubt that ESG-related demands will increase in the near term – directly from activists or from non-governmental organisations with a political agenda on climate change aspects.

That being said, ESG should not hide the other traditional demands regarding governance that will always remain key for activists, as governance and management are central for issuers. The universe of activists is also increasing, with 'traditional' hedge funds, private equity firms and first-time activists becoming bolder and less sensitive to the location of their targets. The activists' main goal should never be omitted: use efficient tools to target any weakness of an issuer to maximise their return on investment.

New topics, new demands, new actors: the dialogue with shareholders, institutional investors and activists is more critical than ever before. It is and remains the most efficient tool to prevent any material disruption for issuers. Institutionalised and more organised dialogue with activists could be on top of the issuers' agenda. Nevertheless, such dialogue is not to be considered as the alpha and omega on how to deal with activists and issuers should always be fully prepared, including for a public confrontation to the extent necessary.

Boards should buckle up for a fraught 2023

Economic pressures are exacerbating the post-pandemic scrutiny of companies' performance. Activists are happier than ever to exploit these circumstances.

This is the third year in which Skadden has collaborated with Activistmonitor to publish extensive research into shareholder activism in Europe. The message of these studies is consistent – boards and management teams that fail to remain vigilant regarding the risk of confrontation with activist investors are likely in for a rude awakening.

In this year's research, that warning resonates louder than ever. Shareholders across Europe endured a difficult period in 2022, with stock markets under pressure as investors digested the implications of higher inflation and a return to tighter monetary policy. Investors are anxious amid these disappointing returns, creating a fertile breeding ground for activist shareholders pushing for change.

Against this backdrop, the post-pandemic rebound in shareholder activism charted in last year's research has continued. This is a theme playing out in other parts of the world, too, including North America and Asia, but European corporates are facing real scrutiny – and more will come during the course of 2023.

Investors are not afraid to be publicly critical of the businesses in which they hold shares – and may often find common ground with other shareholders, including existing ones. The rise of ESG issues is one key part of that story. The move towards sustainability and improved ESG performance can bring companies and their shareholders together and generate value in the long run. But it also increases the possibility of disagreement and disillusionment in the short term, particularly when some businesses already find themselves in dire straits financially.

The bottom line is that activist shareholders will continue to make themselves heard, frequently at a volume that is disproportionate to the size of their stakes in companies. Europe's corporates must be ready.

Our key findings include:

1. Over the last 12 months, 86% of corporates say they have identified new weaknesses that could be raised by activists. Of those, 69% have already broached such weaknesses in discussions with shareholders.

2. 71% of corporates anticipate an increase in shareholder activism over the next 12 months, including 48% who expect a significant increase. Only 3% expect a moderate decrease.

71%

3. Almost three-quarters of respondents (74%) agree that companies should be very concerned about being targeted by UK activists, and the remaining 26% are at least somewhat concerned.

4. Asked to rank what they expect to be the most prevalent activist demands, those relating to changes to the members of the board/ management garner the largest share of primary votes (28%) among our respondents. The next most popular answers are governance structure changes (18%), environmental changes (14%) and anti-ESG demands (10%).

5. 96% of respondents agree that 'activists will increasingly prioritise ESG issues in their campaign demands', and 90% expect the impact of ESG disclosure requirements on activists' demands to increase over the next 12 months.

96%

6. Respondents collectively believe the single most effective defensive tactic that a company should adopt when facing a public campaign is communicating with the activist, which garners 22% of most-important votes.

7. 29% of corporates believe the evolution of the legal framework around public campaigns should focus on disclosing the identity of the activists and certain information on ultimate beneficiaries. Meanwhile, 33% of activists emphasise the need to create a shareholder dialogue platform within each company.

29%

Methodology
In Q4 2022, Activistmonitor surveyed 35 corporate executives from listed companies and 15 activist investors from the UK, France, Germany, Italy and Switzerland in order to gain insights into key trends in Europe's activist investing space. All responses are anonymous, and the results are presented in aggregate. All Activistmonitor figures referenced are correct as of 12 December 2022.

Part 1: 2022 Review Activists pitch 'tough love' for hard times

Proactivity in appraising potential frailties and improving investor engagement are gainful tenets for boards, especially with the arena of shareholder activism becoming more contentious.

After decelerating the year before, 2022 marked a return to form for shareholder activists in Europe, particularly in relation to campaigns brought against companies in the UK and Germany. Overall, the number of open live campaigns in the region reached 341 in December 2022, up 18% from end-2021, according to Activistmonitor data.

That sum included 52 new, still open public campaigns against European companies that arose during the course of 2022. New campaigns in the UK (25, up from 18 the year before) accounted for around half that activity. Germany contributed eight such campaigns (up markedly from only two in 2021), and Switzerland four. For their part, France, Sweden and the Republic of Ireland accounted for three each, with six further countries adding but one apiece.

That cumulative figure of 52 open campaigns represents a year-on-year acceleration of 33% from 2021. The bulk of that activity was front-loaded, with H1 2022 contributing almost three-fifths of new campaigns launched in Europe.

Coming under the most strain were large companies, meaning those with a market capitalisation exceeding US$2bn. These were targeted in 30 campaigns, an increase of 67% from the 18 interventions recorded in 2021 against organisations of this size. Smaller companies came under roughly the same degree of scrutiny as the preceding year: those with a market cap between US$1bn-US$2bn were targeted in five campaigns (the same figure as in 2021), while those under US$1bn logged 17 (just one more than the year before).

The acceleration in the number of public campaigns in Europe generated a corresponding year-on-year increase in the number of demands being issued. These rose to 125, versus the 101 brought in 2021. Specifically, two types of demand comprised the lion's share of proceedings in Europe.

> 2022 saw a number of businesses proactively announce broad "strategic reviews" as a means to buy some time to consider a range of possible corporate options and to build in breathing space to gather input from their shareholders.
>
> Bruce Embley, Partner in Skadden's London office

As was the case in 2021, changes to the board or management predominated, with 26 such demands issued (up 53% from the 17 brought in 2021). Almost as common were demands opposing a proposed acquisition or merger, with 23. This is a massive increase from the last couple of years: 2020 saw just eight such demands, and 2021 only six. Staying on the theme of frugality, the next most common demand concerned cost reductions and operational improvements. Activists brought 18 such interventions, up from just five issued in 2021.

As far the identity of activists is concerned, no one player stood out from the crowd. The majority took only

Live campaigns in Europe

one campaign public, and a handful brought two. These included New York-based Elliott Management and London-based Bluebell Capital Partner – each of which was responsible for five public campaigns in Europe the year before – as well as Artisan Partners (in Milwaukee), Cevian Capital (Stockholm) and Legal & General Investment Management (Dublin).

London-based Petrus Advisers brought three campaigns and was responsible for the greatest number of demands in aggregate with 12. Eight of these involved the activist's campaign against Aareal Bank, the German real estate bank. Their demands were far-reaching, ranging from changes to the bank's board and dividends-related demands to governance changes and opposing a merger.

Different shapes and sizes

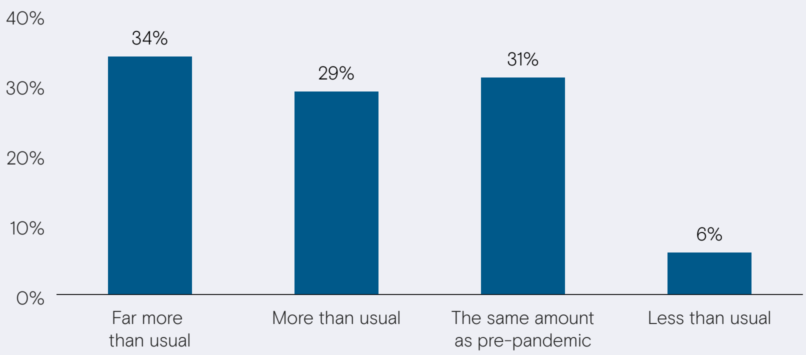
For many European companies, the potential to be targeted by an activist investment campaign presents a real and present danger. Almost two-thirds of corporates in this research (63%) reveal that their boards have talked more frequently about the threat proposed by such campaigns over the past 12 months.

For many boards, the prospect of a confrontation with activists – who are growing in number and in

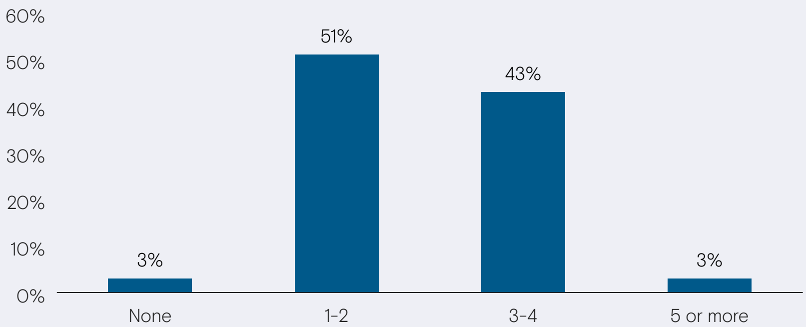
Total campaigns by market capitalisation (live & potential)

Market cap	2021	2022	Growth
<US$1bn	16	17	6%
US$1bn-US$2bn	5	5	0%
>US$2bn	18	30	67%
Total	**39**	**52**	**33%**

Over the last 12 months, how often has your board proactively discussed the threat of activist campaigns? (Select one, Corporate only)



Over the last 12 months, how often has your board been approached (privately or publicly) by activists? (Select one, Corporate only)



ambition – is a very real possibility. Board members are anxious to monitor the emerging threat and determined to be ready to respond when activists do begin to circle.

Just over half of corporate respondents to our survey (51%) say that, over the last 12 months, they have been approached either once or twice by activists, either privately or publicly. That figure is down from last year's report, when 66% of corporates said the same. But that decline is clearly offset by the rise in the number of respondents reporting their having to deal with a handful of approaches from activists over the course of 2022.

Specifically, in the last edition of this study less than a third of corporate respondents (31%) said they had been approached on three or four occasions over the preceding 12 months. This year, that share is up to 43%, indicating that activists have been bolder in taking boards to task over their perceived shortcomings.

It is also the case that boards are increasingly worried about being approached by activists from around the world. Of those corporates targeted by activists over the past 12 months, almost a third (31%) say the approaches had come mainly from non-local investors, up from only 9% in last year's research. As a board member at a UK-based corporate observes, "Location does not matter now, because there are many online means to communicate, and news about the business spreads fast."

Still, local activists remain a concern, with 46% of corporates saying their approaches had split fairly equally between domestic and non-local investors, and a further 23% add that they were targeted largely by the former. The CEO of an Italian corporate warns, "Local activists do take advantage of the proximity to our offices and they are also well aware about the persons they need to approach."

In addition, corporates identify a number of different constituencies of activist investor where activity now appears to be on the rise. For example, 54% of corporates point to a significant increase in contact from hedge funds compared to the previous 12 months; 46% say the same of first-time activists. Private equity funds have also been making their voices heard, with 23% and 57% of respondents describing these organisations as being, respectively, much more active and somewhat more active over the last 12 months.

This appears to be part of a continuing trend. In last year's research, corporates also warned of increasing levels of activity from hedge funds, first-time activists and private equity players. In other words, while activist investors come from disparate segments of the financial ecosystem, a willingness to increase their activity is a commonly shared characteristic.

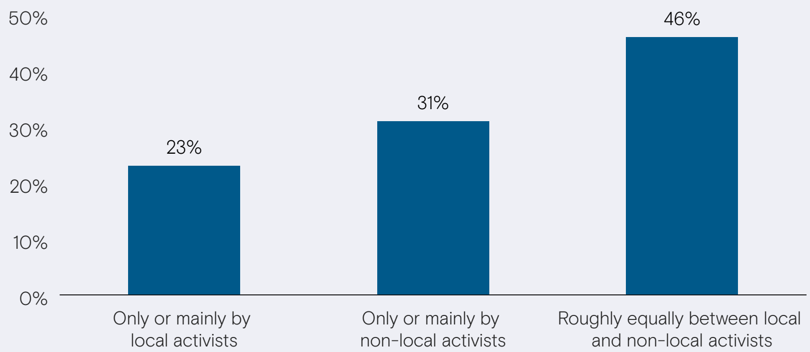
Fighting on multiple fronts

One worry for many corporates is that they are becoming vulnerable to activism on a growing number

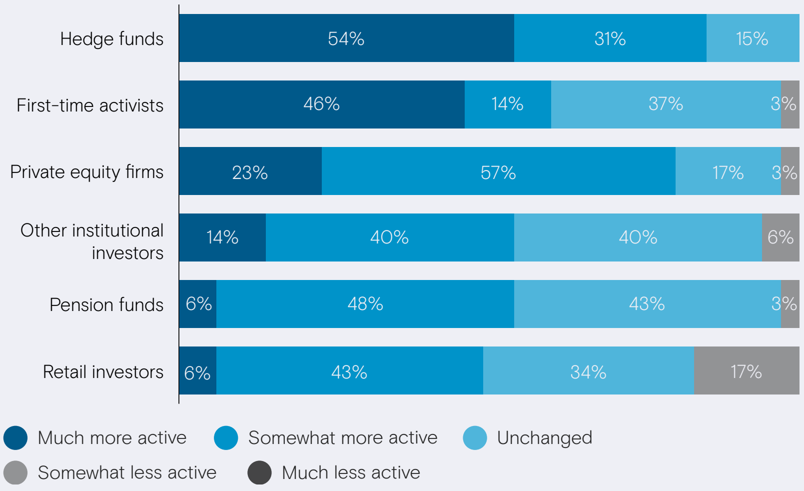
Demands made in open live campaigns

	2020	2021	2022	Y-o-Y 2022
Discussions	7	0	2	NA
Cost reductions/Operational improvements	14	5	18	260%
Share buy-back/Dividend/Return of capital	9	8	4	-50%
Acquisition/Merger	3	3	4	33%
Oppose acquisition/merger	8	6	23	283%
Bolt-on/Divestiture/Spin-off	13	14	9	-36%
Oppose bolt-on/Divestiture/Spin-off	1	4	0	-100%
Strategic alternatives	10	6	11	83%
Capital allocation/structure changes	10	4	0	-100%
Governance changes	15	15	13	-13%
Management/board changes	16	17	26	53%
Board member(s) appointment	22	18	15	-17%
Environmental/social changes	2	1	0	-100%
Total	**130**	**101**	**125**	**24%**

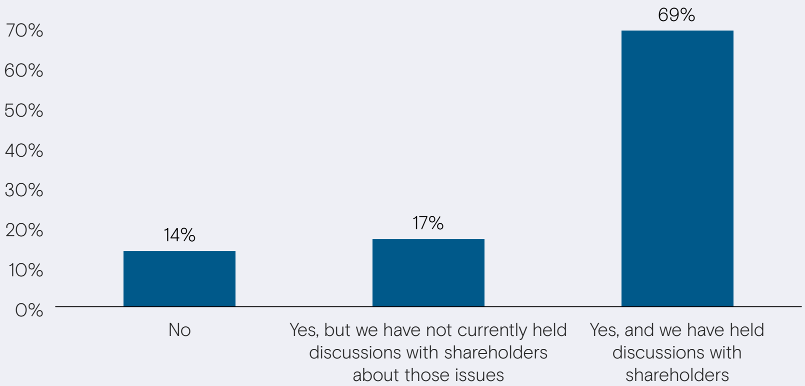
Over the last 12 months, have you been approached mainly by local or non-local activists? (Select one, Corporate only)



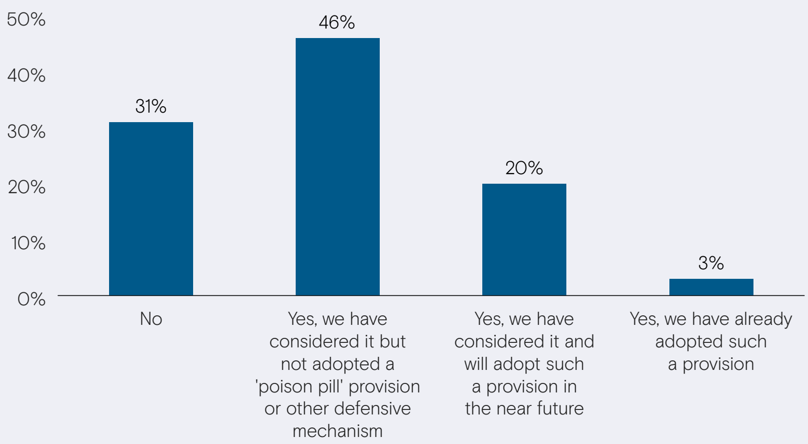
Over the last 12 months, how much more or less active/vocal have the following types of activists been compared to the preceding 12 months? (Select one option for each activist type in the table below)



Over the last 12 months, have you identified any new weaknesses that could be raised by activists in potential campaigns? (Select one, Corporate only)



Over the last 12 months, has your board considered adopting a 'poison pill' type provision or other defense mechanisms? (Select one, Corporate only)



of fronts, with 86% of respondents saying they have identified new weaknesses that activists might seize upon.

The issues that corporates worry might draw activist attention are wide-ranging. "There are a few new weaknesses because of the inflationary environment," concedes a board member at a German corporate. A peer at another Germany-based company adds, "Since there have been regulatory changes, and shareholders anticipate more involvement in activities, it is important to carry out discussions at the proper time."

This final point is an important one. As discussed in more detail in Part 2 of this report, one vital means for boards to mitigate the risk of shareholder activism is to engage more proactively with investors. Better shareholder communication is both a preventive and a defensive measure in this regard.

The other question for corporates concerned about shareholder activism is how precisely to take action to deter campaigns. Some feel that simply identifying potential weaknesses and discussing these issues with shareholders is not a sufficiently robust strategy. Instead, they opt for more aggressive measures. In this year's research, 23% of corporates say they either have 'poison pill' or other defensive arrangements in place to deter activists, or plan to implement them.

This figure, however, is down from 43% in last year's research. In fact, almost half the companies in this year's research (46%) say that while they have looked at the possibility of adopting poison pill provisions or other defensive mechanisms, they ultimately decided not to take this action.

In other words, corporates today seem more comfortable with the idea of heading off a confrontation with activists by being upfront with investors and talking through problems, rather than by adopting mechanisms that may deter a campaign but do not address the underlying cause of anxiety.

Part 2: 2023 Outlook Economic disruption invites relentless scrutiny

Even in turbulent times, shareholders are disinclined to cut companies slack on performance. From dividends to ESG, activists will find ways to pressure boards.

With the near-term macroeconomic outlook darkening, geopolitical tensions rising and stock markets struggling to maintain valuations, conditions are ripe for an escalation in shareholder activism. That is certainly the expectation of respondents to this research, who are anticipating a variety of threats from a wide range of activists and considering how best to defend themselves.

1 Activism on the ascent

"I expect a significant increase in activity," says a board member at a UK corporate, sharing a widely held view, "Shareholders want to see significant changes in the operations management, digital strategies and sustainability strategies overall."

At a German corporate, a board member adds, "There will be a significant increase in shareholder activism because returns are not as favourable as investors had anticipated." Elaborating on the current troubling conditions, a Swiss CEO warns that "the pandemic and inflation risks have affected the output of companies. Many have not lived up to their promises when it comes to financial performance."

Such sentiment explains why almost three-quarters of the corporates in this research (71%) expect to see levels of shareholder activism increase over the next 12 months. That includes almost half (48%) who are anticipating a significant increase.

Still, it should be recognised that these numbers are down compared to last year's research, when 97% of corporates predicted more activism. The expected wave of post-pandemic activity did not materialise entirely – some companies escaped, as we saw in Part 1. That may have tempered expectations for the year ahead, at least to some extent.

> Whilst the macroeconomic issues facing businesses – including recruitment and retention, input cost inflation, supply chain shortages and global political uncertainty – continue to represent a significant challenge to profitable performance, boards should expect very limited patience from activists. Activists will expect business leaders to adapt to face these challenges and find new ways to deliver shareholder returns. And they will not be reticent to criticise leaders who fail to do so.
>
> George Knighton, Partner in Skadden's London office

Similarly, while most corporates expect to see increased volumes of hostile takeovers in Europe over the next 12 months, this view is less widely shared than in last year's research. Overall, just over two-thirds of corporates (68%) forecast a rise in hostile takeovers over the next 12 months, including 37% who predict a significant increase. Those figures are down from 86% and 49%, respectively, a year ago.

Under a microscope

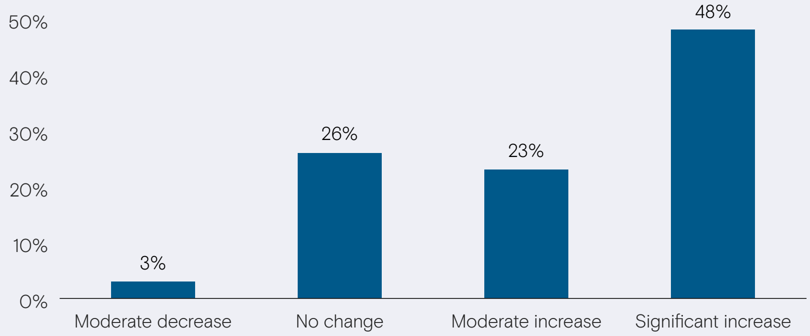
As for the activists themselves, they also expect to be busy. Around two-thirds (67%) expect to take part in three or four campaigns over the next 12 months, with the remainder anticipating one or two. "Activists want major reforms in operational quality and in ESG compliance," says the head of business development at a France-based activist investor.

Activists are likely to coalesce in certain areas. In particular, more than half the activists in this research (53%) cite the UK as the European market where the best campaign opportunities are most likely to present themselves. "Since there have been changes in the political outlook and regulation, it leaves more opportunities for shareholder activism," says the head of business development at a UK activist.

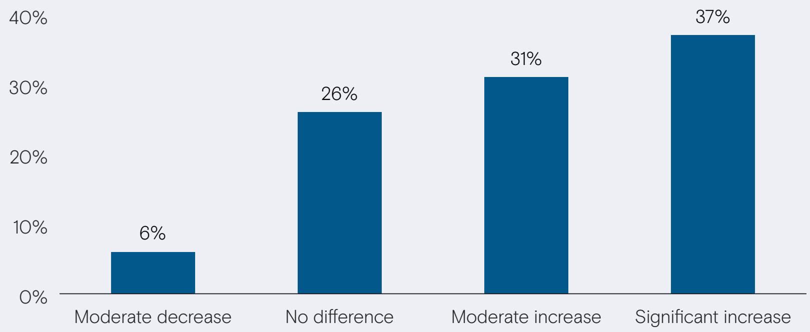
However, corporates in other markets should not expect to avoid entreaties. As the managing partner of a Swiss activist says, "France and Switzerland offer good opportunities. There is more transparency in the business operations there, so activists have better opportunities to identify and raise problems." Indeed, 27% of activists cite France as offering the greatest potential for activity, making it the most popular response after the UK.

As for where the most prolific activists are likely to emerge from, our research suggests European corporates should be especially wary of investors in the UK. Almost three-quarters of respondents (74%) believe corporates ought

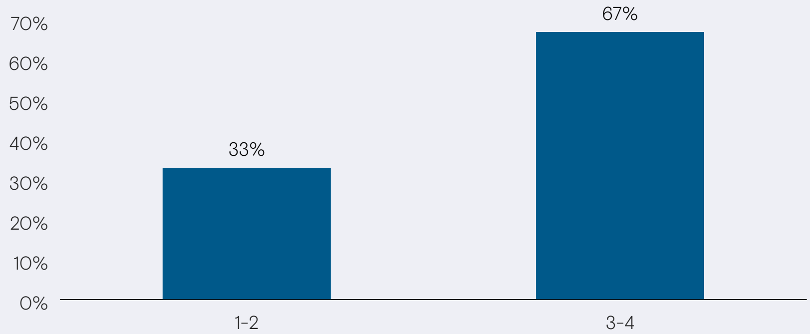
What type of evolution in activity are you anticipating in shareholder activism over the next 12 months? (Select one, Corporate only)



How do you expect the volume of unsolicited or hostile takeovers in Europe to change over the next 12 months? (Select one, Corporate only)



How many activist campaigns do you expect your organisation to be involved in over the next 12 months? (Select one, Activist investor only)



> Today's campaigns cover more 'long' themes, such as strategy and ESG. As a result, activists are increasingly viewed as a representative voice for shareholders, raising their appetite for public campaigns.

Scott Hopkins, Partner in Skadden's London office to be very concerned about UK-based firms, with the remaining 26% somewhat concerned. “UK activists have been more active in raising issues publicly, and this is the main reason for the overall concern,” explains a board member at a French corporate.

There is also a widely held expectation that North American activists will be closely scrutinising the European scene. Almost two-thirds of respondents (64%) see this as a very likely source of activism, including 46% who believe European companies should be very concerned about this possibility. “North American investors are noticing the sudden disruption in economic stability, and there are geopolitical concerns also. This will prompt a reaction,” says a board member at a German corporate.

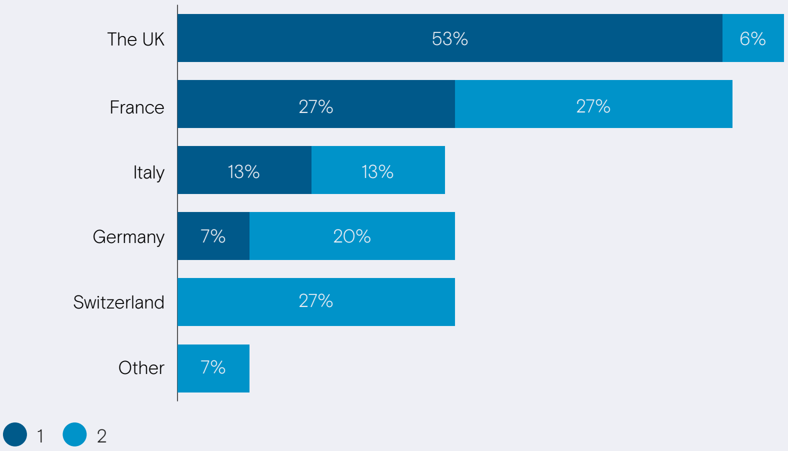
Anglo-Saxon activists have been a thorn in board members’ sides for some time. As the CEO of an Italian corporate puts it, “North American and UK activists have become very vocal about their demands and concerns over the past five years. When they press for changes in the organisation, they do not relent, even after proper justifications.”

Some sectors of the economy are more likely to see higher levels of shareholder activism than others. In particular, 26% of respondents pick the technology, media & telecoms (TMT) sector as likely to see more activism than any other industry over the next 12 months, with a further 28% citing it as their second choice.

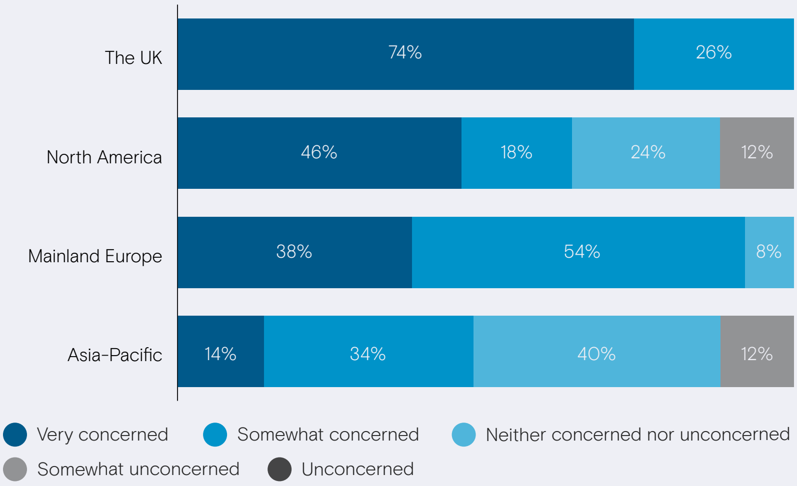
Only the energy, mining and utilities (EMU) sector comes anywhere close to matching the marks set by TMT – 22% and 16% of respondents, respectively, cite EMU as their first and second choice for higher levels of activity over the year ahead.

This has been a recurring theme of our research. In all three iterations of this report, respondents have been most likely to cite TMT and EMU as generating the greatest volume of shareholder activism. It appears the high-growth

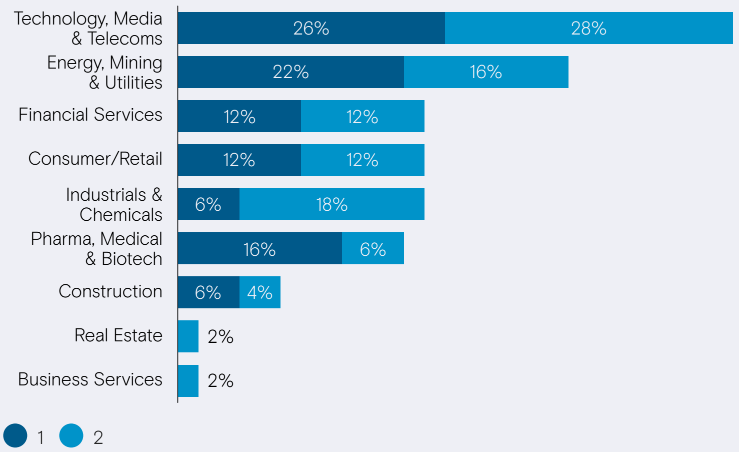
Which European markets do you expect to offer the best opportunities for activist campaigns over the next 12 months? (Select top two and rank 1–2, Activist investor only)



To what extent should companies in Europe be concerned about becoming targets from activists based in the following regions over the next 12 months? (Select one option for each region)



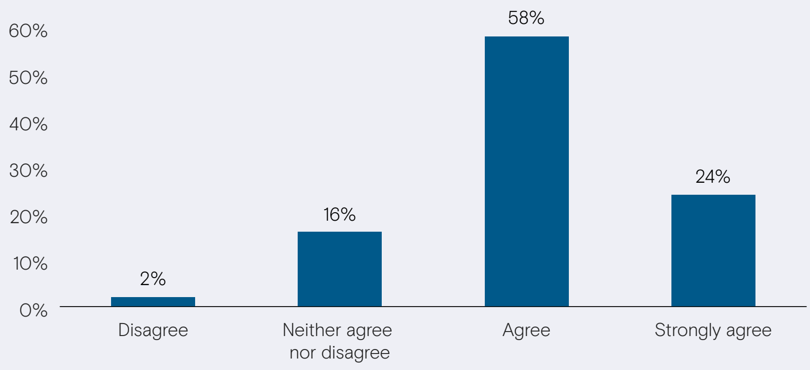
In Europe, in which industries do you expect to see the most activist campaigns over the next 12 months? (Select top two and rank 1–2)



technology space, where M&A activity has remained at elevated levels, is attracting attention from investors concerned about under-performance, too. The EMU sector, meanwhile, has seen substantial volatility as commodity and energy prices have fluctuated, in addition to the ESG-related demands to which the industry can be especially vulnerable.

One other cause for concern among corporates is the widespread expectation that more activist campaigns will enter the public sphere over the next 12 months. More than three-quarters of respondents (82%) share the view that activists will campaign publicly and visibly, rather than working quietly behind the scenes with boards and management teams, to achieve their aims.

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'? (Select one)



This number remains broadly unchanged from last year's research, with both corporates and activists themselves expecting public campaigns to predominate. "There are more chances of the activists' demands being heard when they involve a strategy of visible activism," concedes a board director at an Italian corporate, "They put forward their demands in a systematic manner and this captures social attention." The managing director of a German activist investor adds, "When the information about these demands is public, the people answerable have to respond and provide clarification about their actions. They can't just smooth over the issue without a resolution."

2 Changes at the top

Activists have a habit of making scapegoats of companies' leadership teams. Looking to 2023, our survey respondents certainly expect activist investors to be targeting boards and management teams with requests for personnel changes. More than a quarter (28%) think this type of demand will be more common than any other over the next 12 months.

Corporates themselves may feel this unfair, but they recognise that there is little sympathy for businesses that rely on mitigating circumstances as a defence for underperformance.

"If the board has not been able to create better growth and development opportunities, activists are not interested in the external pressures the company has faced,"

> In the UK, we are seeing more public director campaigns, which can be prolonged and wear down management. This is evidenced by the fact that CEO turnover at European companies within six months following an activist campaign, whether or not the activist publicly demands it, is around 20% per year on average.

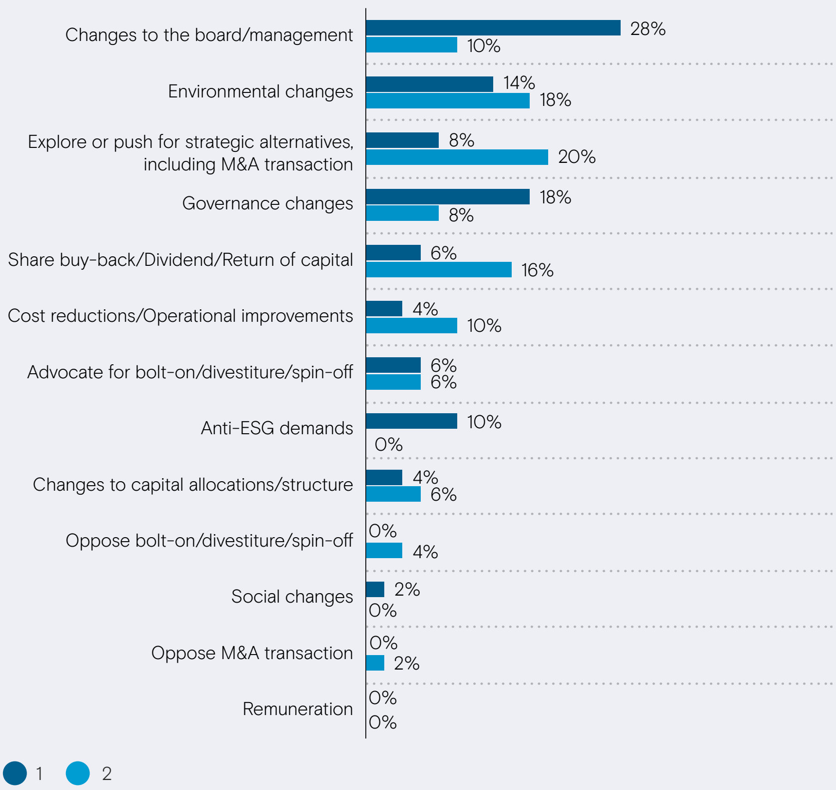
Scott Hopkins, Partner in Skadden's London office says a board member at an Italian corporate. The head of business development at a UK-based activist is blunt about these conditions, saying, “If the current board or management teams are incapable of managing their responsibilities and driving performance, then it is time for a change.”

Still, activists will continue to target businesses in other ways over the next 12 months. Respondents predict that governance (cited by 18% as likely to be the most common focus of activists) and environmental changes (14%) will present flashpoints. Both areas were also highlighted in this research a year ago.

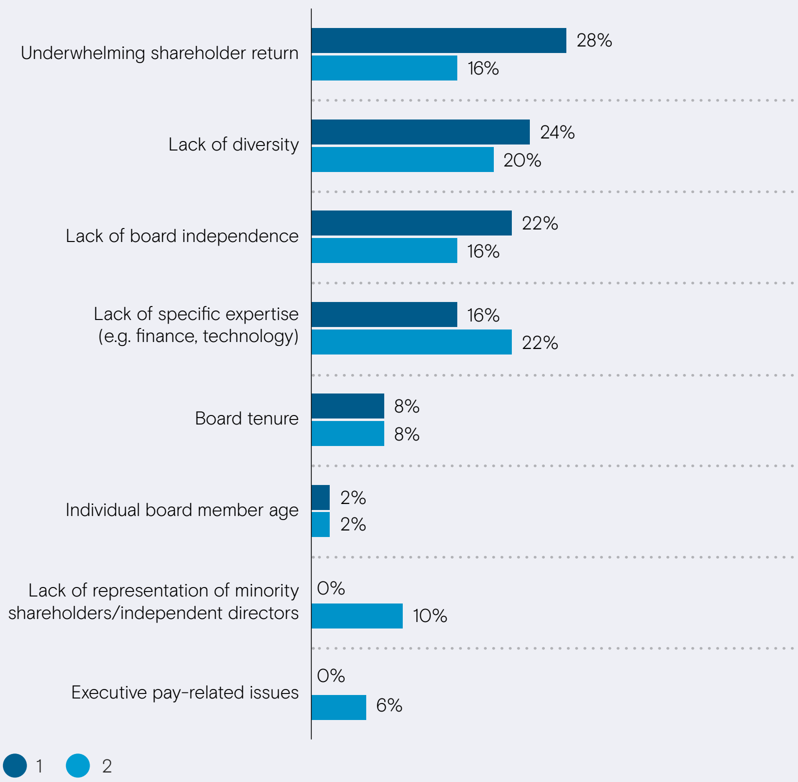
This may reflect the growing interest in ESG issues among a broadening group of stakeholders, including investors. But our research also highlights something of a backlash against the ESG movement. For some investors, moves by companies to take greater account of ESG are undue and points of contention. Indeed, 10% of respondents – the fourth largest share overall, ahead of the 8% citing demands for strategic alternatives and 6% referencing share buy-backs – think anti-ESG demands will be the most likely to come to the fore over the next 12 months.

“Anti-ESG demands will be most prevalent. Companies may be over-emphasising ESG issues, and this has raised concerns in terms of the returns for shareholders,” explains a board member of a German corporate. An Italian CEO adds that “anti-ESG demands have become more common, since there is a negative impact on the overall shareholder value. If too many investments are aligned towards ESG, this may be a concern for shareholders.”

Of the various categories of activist demands, which of the following do you believe will be the most prevalent in Europe over the next 12 months? (Select top two and rank 1–2)



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



Companies must remain cool-headed to understand the ESG changes sought by institutional investors, activists and regulators, and how the various disclosures are shaping up so they can efficiently address relevant concerns.

Armand Grumberg, Head of Skadden's European M&A practice

Market challenges

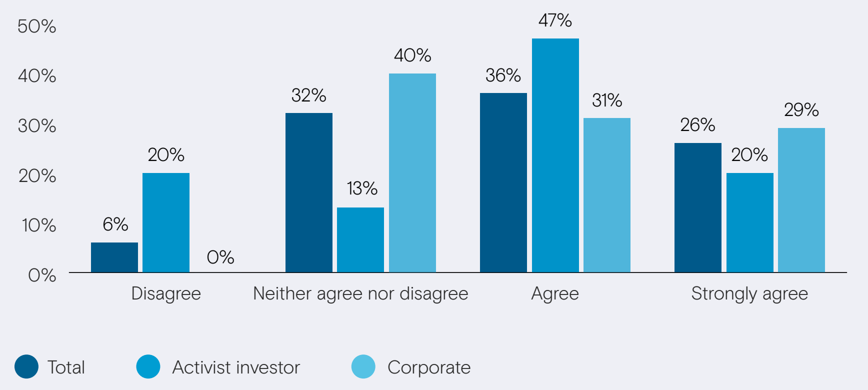
For business leaders concerned about their vulnerability to activist requests for changes to personnel, it is important to understand what might prompt such action. Our research suggests activists may take several lines of argument to justify such demands.

First, 28% of respondents overall, the largest share, argue that underwhelming shareholder returns are the most likely reason that activists would pursue changes to a company's board. But almost as many (24%) believe activists are most likely to use a lack of diversity as a pretence to campaign for change at the top of organisations. Not far behind, 22% suggest that a perceived dearth of board independence could lead to more demands of this nature.

Notably, the answers look a little different when considering only the views of the activists who participated in our research. Among this group, 47% cite a lack of diversity as the most likely driver of an activist campaign for board or management changes. Corporates that are currently performing poorly on this metric should consider this warning carefully.

Alongside these issues, many respondents point to the likelihood of activists pushing for increased rewards. Almost two-thirds (62%) agree that activist investors are likely to focus on share buy-backs and dividend-related issues over the next 12 months, including more than a quarter (26%) who strongly agree.

Do you agree with the following statement: 'Activists will particularly focus on share buy-back or dividend issues in 2023'? (Select one)



Corporates are cognizant that the share price performance of many European companies over 2022 was disappointing. While dividends have recovered in most sectors from the cutbacks seen at the height of the pandemic, there is room for improvement.

"Dividends have been limited and activists will be pushing for buy-backs in these conditions," acknowledges the CEO of a German corporate. A board member of a Swiss company adds, "When a company is capable of participating in buy-backs, it does help increase their share price. That is one reason for activists to focus on buy-backs."

The activists who participated in our study are clear about what they want. "The market challenges are increasing and limiting returns on investments, so buy-backs will be demanded," says the president of a Swiss activist, while a partner at an activist in Italy argues that "the overall financial condition of the company can be improved by way of share buy-backs. If the company is in a good financial position, they can use their resources to retain shares."

Indeed, corporates themselves may be slightly underestimating how strongly activists feel about this issue. While 67% of activist investors surveyed for this research agree activists/their peers will focus on buy-back and dividend issues in 2023, only 60% of corporates take the same view.

3 The ESG revolution

As alluded to in the previous section, ESG-related demands are likely to be a crucial theme in activist campaigns in 2023. Almost every respondent in this research (96%) believes activist investors will increasingly prioritise ESG issues over the coming 12 months, including more than half who strongly agree.

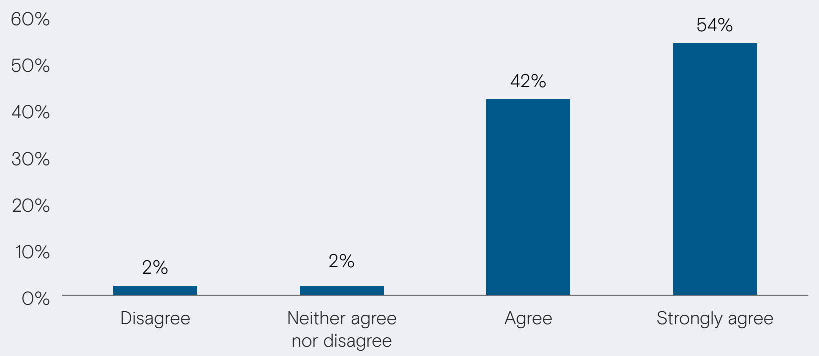
This line of thinking has strengthened since last year's research. In that report, 80% of respondents predicted an increasing focus on ESG among activists. Now that view is near universal.

There are several explanations for this hardening of attitudes. Certainly, some activists appear to believe sincerely that companies are not doing enough to live up to their ESG responsibilities. That position may be informed by different motivations, with some investors focused on the moral imperative for action and others more worried about the financial or regulatory consequences of failing to move quickly. Whatever their starting point, it is an important driver.

"Activists are increasingly concerned about the impact that corporates are having on the environment and society. They want to see companies taking environmental issues more seriously," says the managing partner of an activist investor in France. In the same country, the head of business development at another activist adds, "We are concerned about the efficiency of companies in this regard. Many are not focusing on ESG issues, and they are only planning enough to comply with the regulatory requirements."

A related issue is a growing concern about companies being chastised for exaggerating their ESG credentials. "Companies are involved in greenwashing activities. This is not a positive sign for the long-term future," complains the managing partner of a Swiss activist investor.

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



It is also the case that many activists see upside potential for the businesses in which they have invested if these companies are able to develop a competitive advantage through their approach to ESG issues. "In many markets, ESG priorities are differentiating companies from their competitors. It has become a tool for the market," says the CEO of an Italian corporate. In these conditions, it is unsurprising that activists are prioritising ESG in their campaigns.

The other factor to consider is the very broad range of issues that fall under the ESG umbrella. Corporates are under pressure to reduce their carbon footprints – many face demanding targets on sustainability net-zero emissions – but they must also take action to improve performance on issues ranging from human slavery in the supply chain to diversity and inclusion within their own organisations.

"There are many sustainability issues that are being raised by shareholders," says a board member of a Swiss corporate. "According to them, companies have not been focusing on sustainability. They want more ESG factors to be incorporated into the company's policies."

Held to a higher standard

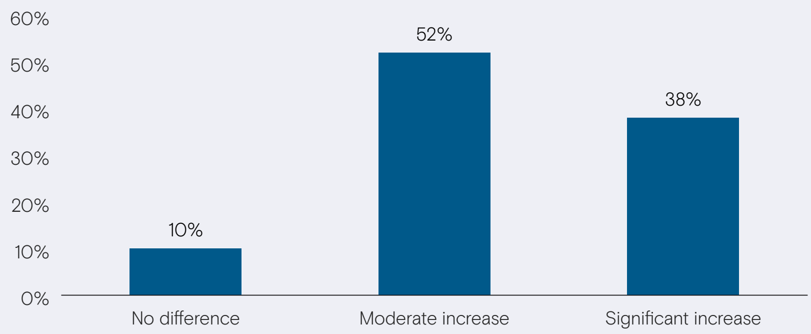
Another important driver of the increasing predominance of ESG in activists' demands is the growing determination of policymakers and regulators in Europe to confront sustainability-related issues and raise disclosure standards.

The European Union is discussing multiple proposals for extending ESG disclosure requirements for all industries, mirroring the progress made in parts of the financial services sector. The UK has already implemented ambitious disclosure rules and plans to go further. The work of the Taskforce on Climate-Related Financial Disclosures is also stoking the flames of reform.

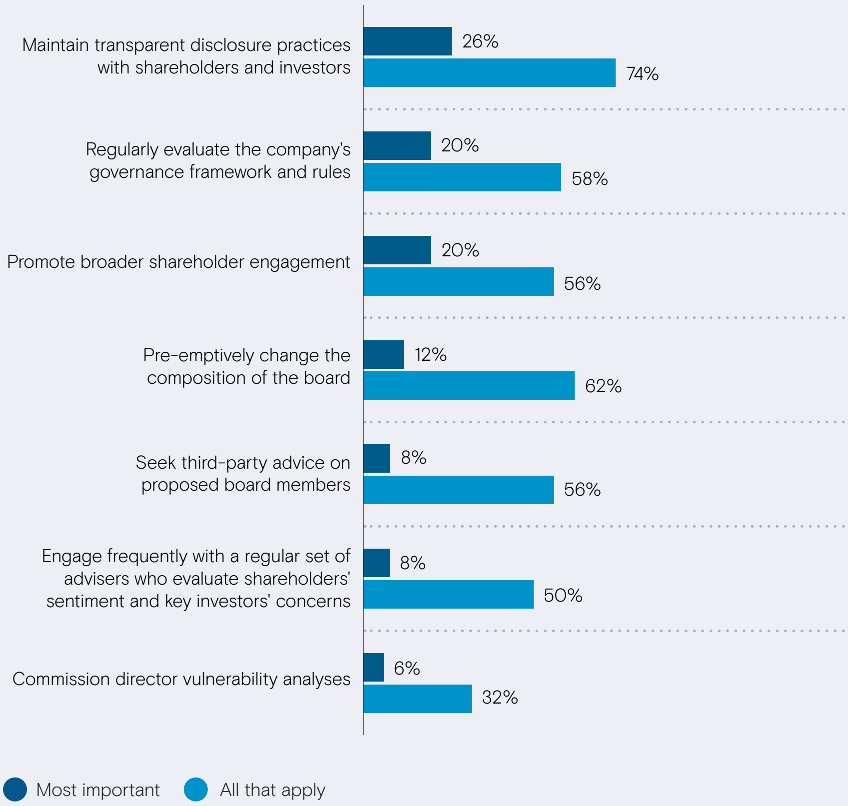
In light of these and similar developments, 90% of our survey respondents believe that ESG disclosure requirements will lead to a rise in activists' demands over the next 12 months. That includes more than a third (38%) who expect to see a significant increase in impact from ESG-related demands owing to the evolution of disclosure regimes.

Some activists seem worried that corporates are not keeping pace with the speed of regulatory change. They expect boards to do better in order to keep up with that evolution. These stakeholders also want better standards of disclosure to investors themselves, so they can compare and contrast performance more easily.

What impact do you believe ESG disclosure requirements will have on activists' demands over the next 12 months? (Select one)



In your view, what are the most effective preventative measures that companies can use to mitigate the chances of activist campaigns? (Select all that apply and the most important)



"Companies are not following suitable standards concerning ESG disclosures. It has become very difficult to compare the performance of different entities," warns the president of an activist investor in Switzerland. A partner at a UK activist points out that leaders on disclosure should enjoy positive benefits, saying, "Activists want to see more transparency in the ESG reporting and disclosure methods. This should have a positive impact on the company's ESG ratings."

As for corporates, they recognise the imperative too. "ESG disclosures have become an important topic for activists," concedes a board member at a Swiss corporate, "They are referring to more structured and streamlined disclosures so that evaluations will be easier for them." The CEO of a German corporate adds, "Different companies and regions are practising different disclosure methods and formats, and this is a major concern for activists. They want to see us use more standard applications."

4 Forewarned is forearmed

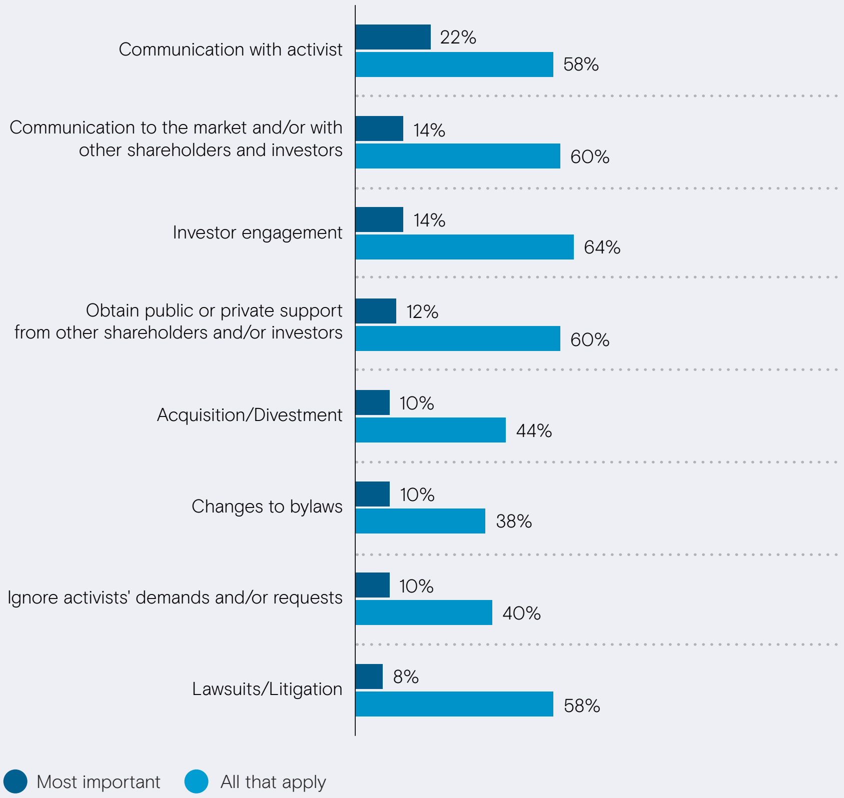
Given their expectations of increasing shareholder activism, how can corporates reduce their chances of facing potentially dangerous activist campaigns? In this research, respondents stress the importance of various types of communication and information sharing with stakeholders.

More than a quarter of respondents (26%, the largest such share) say the single most effective preventive measure that corporates can take is maintaining transparent disclosure practices. If they are as open and honest as possible about performance, operations and other issues, shareholders will be less likely to lend support to activist interventions.

Both sides of the debate share this view. "Shareholders should not feel that the company is maintaining secrecy about their capabilities in any way," says the partner of an activist investor in Italy. And according to a board member at a German corporate, "Transparent disclosure practices would increase the trust between companies and their shareholders. The latter will not feel as though the company is withholding key information about any aspect of the business."

Relatedly, 20% of respondents suggest corporates engaging regularly with shareholders is the most effective way to prevent being targeted by activist investors. Clearly, when shareholders feel their views are being heard, there is less room for the misgivings that might spur a campaign to develop. "When we know that investors want to voice their opinions, it is

What are the most effective defensive tactics that companies use when faced with a public activist campaign? (Select all that apply and the most important)



better to promote shareholder engagement. We can provide a better way for them to communicate with the organisation," says the CEO of a German corporate.

Similarly important, also being cited by 20% of respondents as a crucial preventative measure, is corporates' readiness to regularly evaluate their governance rules, in order to ensure they have a framework through which the board and management is held suitably accountable. "This can show the company's willingness to change in line with the latest trends," says a board member at an Italian corporate.

Aligning with allies

Inevitably, however, companies will have to contend with activist campaigns, including, on occasion, public confrontation. In which case, the business will need to identify the most effective tactics to defend itself against such threats.

Engagement, both directly with the activist and with the broader shareholder base, is critical. More than a fifth of respondents (22%, the largest such share) say direct communication with the activist is the most effective defensive tactic. Communication with other shareholders (14%) and, relatedly, broader investor engagement (also 14%) are identified as the next most effective defensive tactics when trying to see off a public campaign.

"Activist investors' role will diminish with increasing engagement," admits the senior partner of a Swiss activist investor, "The issues will be addressed at the core when companies and their investors conduct open and honest discussions."

Corporates will also want to consider that different groups of investors feel differently about activist campaigns, and that these views can change over time.

On the one hand, around half of respondents expect institutional investors to be accepting of activists over the next 12 months (48%, though that is down markedly from the equivalent figure of 96% recorded in last year's research). By contrast, respondents think retail investors are likely to be opposed to activist activity – 50% think their attitude will be weighted towards intolerance of public campaigns.

Boards of directors and management teams, naturally, are widely expected to be very intolerant of investor activism. But by engaging with other key groups sharing this view – such as retail investors – corporates may be able to oppose activists more effectively.

As for institutional investors, here too there may be scope for corporates to win support – 30% expect intolerance towards activists, and it would be prudent of boards to capitalise on that distaste for public campaigns. Specifically, 42% of respondents agree with the suggestion that increased engagement between companies and their large institutional investors can mitigate activists' influence.

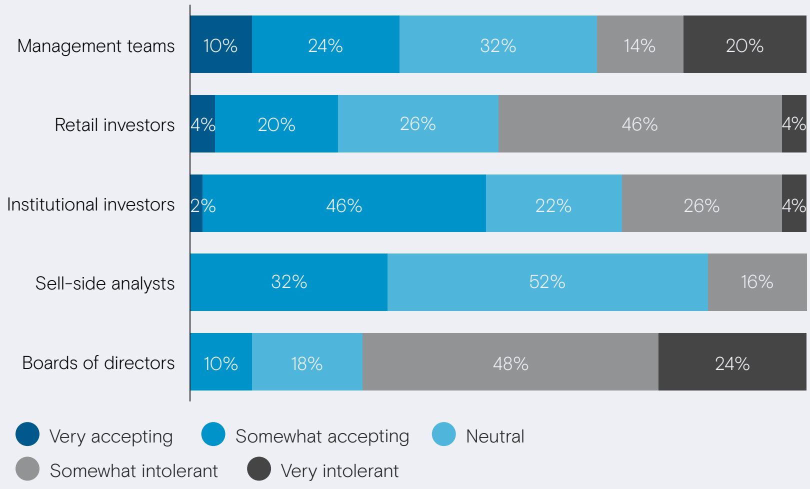
This makes sense. Where corporates have strong and trusting relationships with their largest shareholders, activist campaigns will find it harder to gain traction. Still, not all respondents agree – 38% suggest engagement may not have the desired effect in this regard.

In the first camp, the CEO of a German corporate observes that "institutional investors have major shareholdings and cannot refrain from making demands. When these are heard as a part of increased engagement, it would be beneficial for companies and activism will decrease." There will simply be less space for activists to press their case, the CEO suggests.

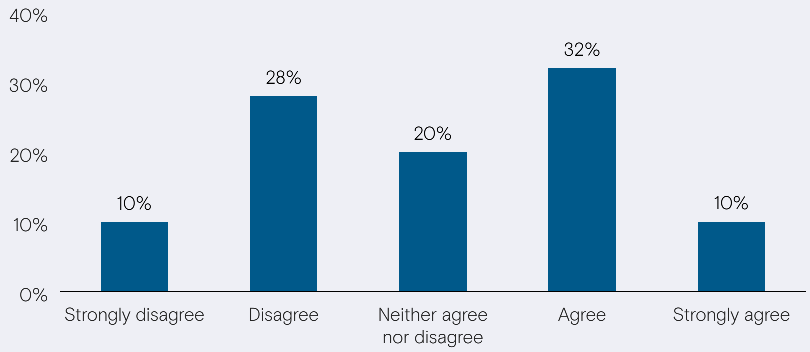
However, the president of an activist investor in Switzerland rejects that line of argument. They warn that increased engagement with large investors "does not guarantee that activism will diminish. Engagement could help in resolving smaller issues, but when major changes are needed, activist investors can drive these changes."

Moreover, some respondents are worried about conceding too much influence to such institutions. "It would give these large companies too much power," says a board member of a German corporate, "Their list of demands will keep on increasing, and they mostly have their own returns in mind. We have to take the company's long-term interests into account."

Over the next 12 months, how accepting or intolerant do you believe the following stakeholders will be of activist investors and public campaigns? (Select one option for each stakeholder type)



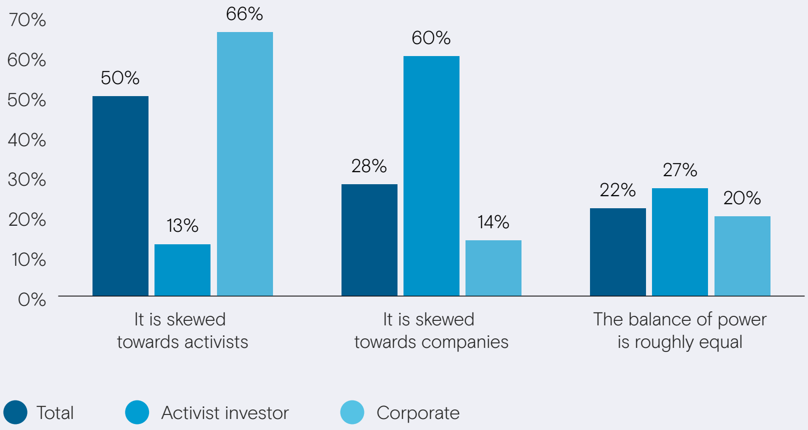
Do you agree with the following statement: 'Increasing engagement between large, institutional investors and the companies in which they control major shareholdings will greatly diminish the role of activist investors.' (Select one)



Aligning with key investors starts with knowing the shareholder base and interests involved. This includes regular exchanges about business strategy, activists and their potential lines of attack and can extend to securing support in the context of transactions.

Matthias Horbach, Partner in Skadden's Frankfurt office

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



5 The imbalance of power

Activist investors and corporates understandably hold different views about who holds the upper hand in their relationships. For corporates, concerned about the disruption that campaigns often create, the natural response is to feel embattled. Equally, activists believe they are pushing for essential changes and point to their minority stakes as leaving them relatively powerless. Adversarial situations only add to the strength of feeling on both sides.

In this research, two-thirds of corporates (66%) complain that the balance of power is skewed towards activists. Almost as many activists (60%) argue the opposite is true. Such views are not set in stone – 20% and 27% of corporates and activists respectively think the balance of power is roughly equal – but this sort of entrenchment can set the tone as campaigns progress, with both sides feeling they are at a disadvantage. The danger is that potentially beneficial exchanges of views become tinged with bitterness.

Resolving these conflicts will not be easy. With such different opinions about who holds the greater power, it is unsurprising that activists and corporates take a different view of how the legal framework around shareholder rights and investor campaigns should evolve.

For corporates, the biggest single cause of concern today is that the law is not sufficiently strong on the subject of forcing activists to disclose their identities and the identities of beneficiaries. Almost a third (29%) want to see tighter laws in this area over anything else, against not a single activist in this research who views this as a priority.

> While many corporates already use some sort of a shareholder dialogue platform in connection with an AGM via their websites, there is hesitation to establish a platform that allows for a broader institutionalised two-way dialogue.

Holger Hofmeister, Partner in Skadden's Frankfurt office

"The ultimate beneficiaries could be different from the information that is being portrayed by activist investors," says a board member of a Swiss corporate. "Disclosures should be a legal requirement for activists so that companies would understand the reasoning behind demands."

Corporates would also like to see activists legally required to enter into a defined period of dialogue before going public with an activist campaign – 26% cite this as the top desired change. "This gives the company an opportunity to respond to the activist's demands in a systematic manner," argues a board member at a German corporate.

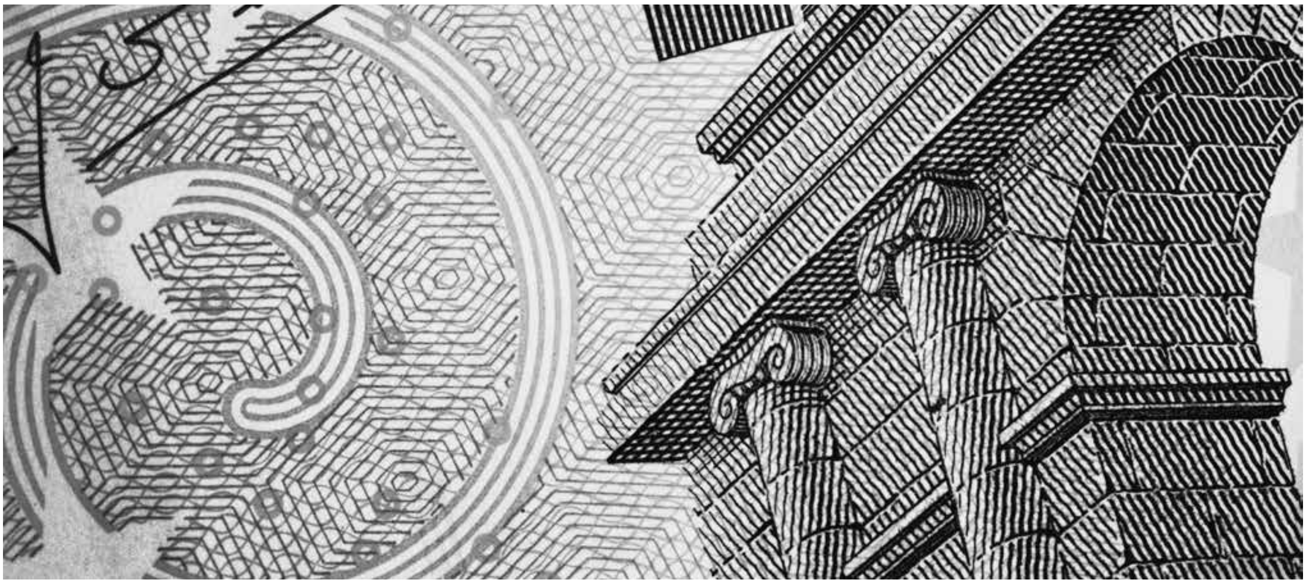
At least on this point, there is some alignment with activists, with 13% citing this issue as a priority for reform. "There could be a dialogue period to get preliminary information or explanations," says the managing director of a German activist. "If this helps resolve issues proactively, then the public campaign can be avoided."

Still, most activists hold different views on what is important. Above all, a third (33%) say they most want to see companies create more formal platforms for shareholder dialogue, in order to facilitate discussion and resolution. Only 14% of corporates consider this worthwhile. Elsewhere, more than a quarter of activists (27%) point to the need to extend provisions governing false or misleading information published by corporates. Here, only 20% of corporates feel as strongly about this issue.

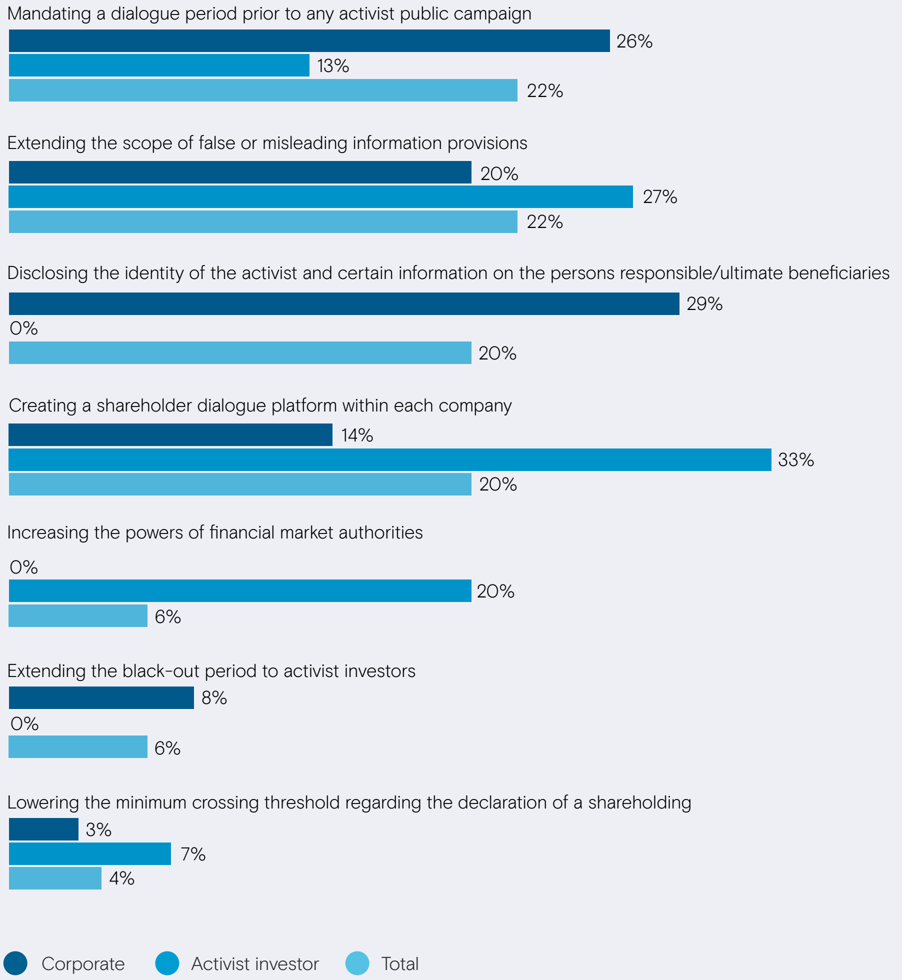
"A shareholder dialogue platform within each company could really assist in addressing key issues on time," says the partner of an Italian activist. "There would be no need for prolonged discussions and issues could be resolved systematically." A board member at a Swiss company is sympathetic to this line of thinking, saying, "Creating a shareholder dialogue platform would be favourable for all parties. It would be easier to put forth concerns and share regular updates about resolutions." Perhaps there is room for an entente to be struck in this area.

> New climate-related disclosure requirements introduced in the UK in April 2022 are likely to fuel both further ESG and anti-ESG activist campaigns. These new requirements will impact most listed UK companies, and we expect them to be a priority for UK plc boards this year.

Bruce Embley, Partner in Skadden's London office



On which area do you believe the evolution of the legal framework should focus with respect to activist investors and public campaigns? (Select one)



Rules of engagement

This research suggests that shareholder activism is set to rise in Europe over the next 12 months. As companies attempt to navigate an increasingly fraught economic environment, activists are likely to push for operational change, reduced costs and new routes to growth, including transactional activity. The clamour around ESG also provides support for the trend towards increased activism.

"We will see more new activist investors coming forward to raise issues in Europe," predicts the CEO of a French corporate, "Considering the geopolitical factors that are affecting supply chains, new investor activity is bound to increase. Shareholders are concerned about the impact on their returns." A German corporate's CEO adds, "The potential economic threats will prompt more activist investors to come forward and demand information on growth, development and financial sustainability."

In some cases, this anxiety around the near-term economic outlook will feed through into investors demanding more upfront rewards, including dividend increases and more share buy-backs. "Some companies have lost their ability to raise profits and create more revenue streams that are beneficial to shareholders," warns the CEO of a Swiss corporate.

Activists are increasingly likely to prioritise environmental and social issues in their demands, positioning themselves as 'responsible investors'. In a few cases, their motives may be entirely sincere, but some may look to exploit the ESG movement to support their more mercenary-like approaches to pursuing change at companies.

"In Europe, the incorporation of the United Nations' Sustainable Development Goals will accelerate. Activist investors are increasingly focused on this topic, and their campaign demands will touch on this issue more often," points out a board member at a UK corporate. Across the Channel, the CEO of a French activist warns that companies will be held to account in this area, "Issues of greenwashing have become more prominent in Europe, and this will drive many activist campaigns. Activists will demand evidence to prove that companies have actually implemented the ESG strategies they claim."

Against this backdrop, the stage is set for another year of combative shareholder activism in Europe. Well-managed companies that plan ahead and prioritise investor engagement will be best placed to see off these threats and to resolve grievances as they emerge, or, ideally, before they even have a chance to surface.

> Boards will be held to account on new routes to growth and on ESG. They should insist that management conduct in-depth analyses to anticipate such demands in order to identify, and propose remedies for, potential weaknesses.
>
> Armand Grumberg, Head of Skadden's European M&A practice

Key takeaways:

1. Companies face attacks on all fronts. Broadly speaking, an increase in shareholder activism should be anticipated in Europe in 2023. Additionally, the variety of activists with which boards must contend is expanding – hedge funds, private equity firms and first-time activists are becoming bolder, and, as one respondent puts it, "Location does not matter now." Boards will have to be more discerning, vigilant and proactive than ever before.

2. Engagement is everything. Although they already appreciate the benefits of discussing concerns with shareholders, with inflationary pressures, geopolitical upheaval and general economic disquiet weighing on investors' minds, boards must double down on this mode of engagement. Installing a more formal and regular engagement platform may go a long way towards assuring shareholders that their voices are being heard.

3. ESG is omnipresent. Activists' motivations for focusing on ESG matters may vary – and may not always be as transparent as they may claim, or so earnestly concerned with sustainability or diversity. But ESG-related demands are only becoming more pronounced. Activists will seize on any shortcomings in this space, so it is crucial for boards to get ahead of criticism or risk of reputational damage by facilitating thorough and transparent disclosure practices.

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 defence. 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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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.