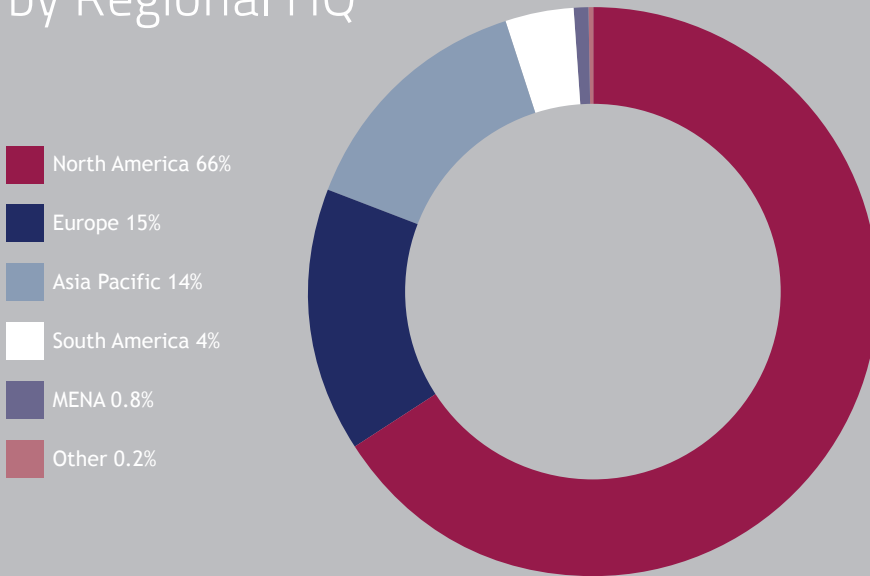


UNLOCKING VALUE: THE POSITIVE ROLE OF ACTIVIST HEDGE FUNDS

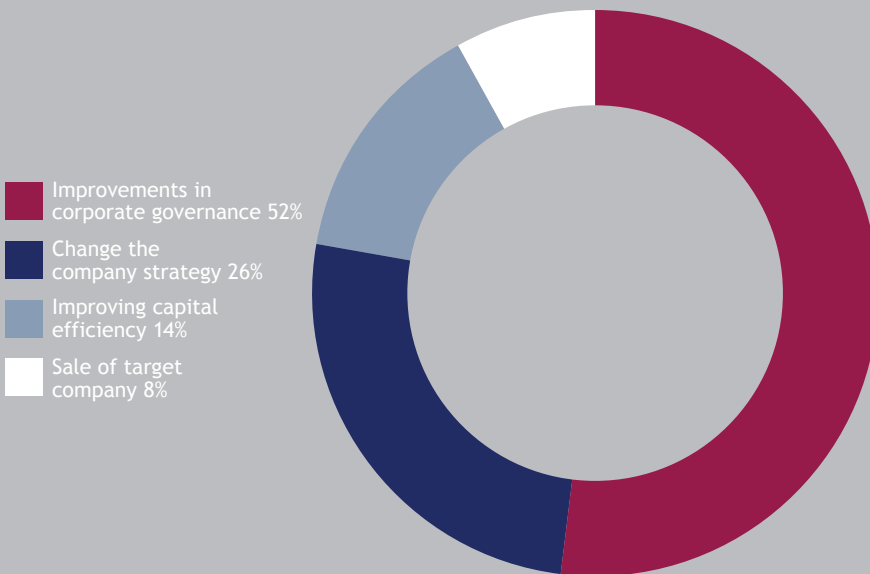
At a glance: Activist hedge funds

Global breakdown of Activist hedge funds by Regional HQ



Source: Preqin

Activist hedge fund objectives



Source: AIMA Research, Activist Insight

\$120 Billion

ASSETS UNDER MANAGEMENT BY
ACTIVIST HEDGE FUNDS

165

NUMBER OF ACTIVIST HEDGE
FUND MANAGERS GLOBALLY

+50%

COMPOUND RETURNS OF ACTIVIST
HEDGE FUNDS FROM 2012-2014

2 Years

AVERAGE HOLDING PERIOD OF
INVESTMENTS BY ACTIVIST HEDGE FUNDS

25%

AVERAGE INCREASE IN SHARE PRICE
OF TARGET COMPANY OVER TWO-YEAR
PERIOD FOLLOWING ACTIVIST SALE

Introduction

They have been called “capitalism’s unlikely heroes¹”. They are the keys that unlock value in public and private enterprises. Activist hedge funds are widely recognised as delivering significant gains to their investors, to the companies in which they invest, and ultimately, to the broader economy.

By taking significant but non-controlling stakes in companies, and holding those positions often for years at a time, activist hedge funds are supporting improvements in the performance of thousands of firms around the world. Struggling businesses are being turned around, well-run businesses are improved, capital more efficiently allocated and the interests of managers, shareholders and other stakeholders better aligned.

Influence on company boards and management is usually exerted by activists in a spirit of collaboration and constructive engagement. Contrary to popular belief, and notwithstanding a few highly publicised cases, adversarial interventions are rare.

The success of these campaigns can be measured in a number of ways. One is simply in the growth of the activist hedge fund sector, which has enjoyed a six-fold increase in assets under management over the last decade. This growth has been driven largely by demand from institutional investors including public and corporate pensions, sovereign wealth funds and endowments.

Another, perhaps more significant measure, relates to the positive impact of activist campaigns on the targeted companies themselves, both during the holding period and following an exit by the activist via a sale of that stake.

We have explored this activity and sought to quantify its impact in a paper we have produced in conjunction with the law firm Simmons & Simmons. The full paper can be downloaded at - www.aima.org/en/education/activism-and-alternative-investment-management.cfm.

What the research shows is that activist campaigns lead to corporate governance reforms, increases in share price and improvements in operating performance. It also shows that activists leave a positive and lasting legacy, with companies continuing to perform strongly even after an exit has been achieved.

All in all, Activist hedge funds are creating a more efficient allocation of an economy’s resources and in turn higher economic growth. Heroic - perhaps. Beneficial - without a shadow of a doubt.



Jack Inglis, AIMA CEO

The paper’s key findings at a glance

Activism yields long-term improvements in performance

Activist engagement by hedge funds is positively correlated to improvements in the share price and operating performance of targeted companies, including after the funds have exited.

Activism leads to greater alignment of interests

Activist hedge funds seek higher standards of corporate governance, which improves alignment of interest between management, shareholders and other stakeholders and ultimately leads to improvements in the efficient allocation of capital and resources in the economy overall. This is one of the main benefits of capital market financing as opposed to bank financing.

Improvements are even seen at companies not yet targeted

The increased likelihood of engagement by an activist hedge fund often leads company managers and boards to make proactive changes to corporate policy that, in general, appear to increase shareholder value and longer-term profitability of yet-to-be-targeted firms.

Activist hedge funds invest for the long term

Activist hedge funds hold investments for longer periods than is common in the market. Such funds have investment horizons averaging around two years, while the average market-wide holding period of stocks is around three months.

Activist hedge funds are mostly collaborative in approach

Contrary to popular belief, most activism by alternative investors takes the form of low-profile interventions and “soft” strategies, such as seeking board representation with management support. Collaborative engagement also appears more likely to achieve success than more assertive approaches, particularly outside the US.

Hedge funds generally make proficient activists

By comparison with other shareholders, activist hedge funds are generally more successful in effecting change and more frequently able to drive profitable improvements in targeted companies.

Activism Explained

1. What is shareholder activism?

Shareholder activism can be demonstrated through taking an equity stake in a company and then trying to influence the company's board or management to adopt its proposed changes. Often the activist accomplishes this through taking a small equity position (~5%) and then encouraging other shareholders to support its proposals.

2. What is the aim of activism?

Activist hedge funds seek to influence a company, rather than control it (as is the case with private equity funds). The activist hedge fund manager seeks a course of action that will unlock value in the share price and transform the long-term prospects of a target company. Courses of action include improvements to governance, shifts in company strategy and reforms to the capital structure.

3. How do companies respond to activist involvement?

Companies often engage constructively with the activist, meeting the activist and agreeing on a set of measures. Often the issue might be put to a shareholder vote. Only if relations break down would the activist solicit proxies or explore legal avenues.

4. What do companies targeted by activist hedge funds have in common?

Target companies tend to have suffered from poor governance structures or exhibited shortcomings in business strategy. However, even the most successful companies can be targeted if an activist perceives that opportunities are being missed by management.

5. Where does activism occur?

While shareholder activism is still predominantly a course of action pursued in the US, it is increasingly gaining popularity across Europe and Asia.

About AIMA

The Alternative Investment Management Association (AIMA) is the global representative of the hedge fund industry. We represent all practitioners in the alternative investment management industry, from hedge fund managers to legal and accounting firms. AIMA is committed to developing industry transparency, industry skills and sound practice, and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA).

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