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FROM THE INSIDE OUT

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"AAA" Report, European Activism

Shareholder activism adapts and evolves to be a growing force across Continental Europe

Whilst the UK remains Europe's single largest hunting ground for activists, they are increasingly turning their sights on Continental European companies. Early signs show that they are successfully honing their tactics to better suit different European markets – often taking a less confrontational approach than traditional U.S. campaigns.

These findings come from the latest refresh of the A&M Activist Alert ("AAA" – a multi-layered statistical model with a 60 percent prediction success rate) which predicts continued significant growth of activism across the continent, with the key sectors to watch identified as industrials and technology.

In all, 150 European companies have been identified and predicted to become the target of an activist approach in the next six to eighteen months if they do not take rapid transformation action. The AAA analysed 1,473 companies with a market capitalisation of at least U.S. $200 million based in the UK, Germany, France, Spain, Italy, Scandinavia, Benelux and Switzerland.

In the previous AAA report in (November 2018), a similar number of companies (148) were identified as potential targets over the coming six to eighteen months, and of those, 21 have already become so, including BT Group in the UK, Agfa-Gevaert in Belgium/Germany as well as German pharmaceuticals giant Bayer.

Looking ahead, the key themes and trends recognised in this latest AAA refresh include the following:

- M&A is becoming an increasingly common feature of activist campaigns. In 2017 and 2018, 12 percent of demands made by activist investors related to potential M&A – this has risen to 17 percent during the first three months of 2019. A clear driver for this trend is the large number of calls for conglomerates to sell underperforming divisions and focus on core activities.
- Industrials continue to be the most predicted target sector for activists in Europe, in part due to the high proportion of conglomerates that are classified in that sector.
- Technology firms are also predicted to be a key sector to watch. SAP, Just Eat and Allied Minds are recent examples of activist action. The high price-earnings ratio ascribed to the technology sector is seen as one of the key drivers behind this trend – every additional € or £ that can be added to bottom line performance should result in relatively greater share price rises.
- Consumer companies have continued to become less attractive to activists. A key factor behind this is that many offline retailers are now too distressed to attract activist interest.
- If they wish to avoid public activist actions, corporates continue to have less than two years from when they first show weakened performance to demonstrate tangible improvements in their published results.
- A key trend expected to grow in the coming years is the emergence of activists seeking to take companies private. This allows them to retain the full benefit of improved performance rather than holding a minority public stake and so sharing any benefit with other shareholders.

"It is clear that activism across Europe continues to evolve", says Malcolm McKenzie, head of European Corporate Transformation at A&M. "No sector is immune, and where activists identify potential opportunities to drive increased shareholder value, they are increasingly adept at adjusting their approach to win over other stakeholders and be seen as constructive partners – less Barbarians at the Gate and more positive forces for change."

Looking at the split by country, the UK remains the biggest market for activists in Europe, with 52 companies identified as predicted targets for an activist approach. Interestingly there has been no clear impact from Brexit uncertainty thus far. However, any continuing disruption is likely to create opportunities for activists, as companies that do not manage disruption well begin to fall behind their peers. A weaker pound could also make UK companies more attractive as buyout targets for foreign investors.

By contrast, more companies are becoming activist targets in Germany and France: 23 German companies are predicted to receive an activist approach, up from 18 a year ago, and in France, the number has increased to 20 from 17 last year.

"Although the UK is still the most targeted market, Germany is catching up," says Patrick Siebert, Managing Director with A&M in Hamburg. "This must alert German management and supervisory board members to ensure that they fully recognise and rise to the challenge. The recent, almost unprecedented, refusal of investors to show confidence in the Bayer executive management is an example of how times are changing."

This continued expansion of activism across Europe demonstrates that historic tactics aimed at defending against activist investors are steadily falling out of favour. It is increasingly the case across all of the continent that acting quickly to improve results and shareholder returns is the most effective way to see off an activist challenge, according to Mr. McKenzie.

"Boards must hunt out areas of sub-par performance and drive a program to ensure that they are demonstrating maximum shareholder value and long-term thinking," he says. "The best defense against an activist is planned and enacted not in the battle, but at least two years earlier when underperformance typically starts."

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