Handelsblatt (November 27, 2017): „New Alliances“ (Translation from the German original „Neue Verbündete“). Author: Peter Köhler und Robert Landgraf.

Headline: New Alliances

Sublines: Activist Hedge Funds Now Wield Greater Influence In German Boardrooms. And They Are Also Partnering Up With Established Fund Companies

One tough old battle is raging out there. First, investor White Tale scuppered the planned $20bn merger between Clariant and US company Huntsman. And, now, it is putting the screws on the management of the Swiss specialty chemicals company. The major shareholder is demanding that its stake in the company – most recently put at just over 20 per cent - be rewarded with three seats on the board of directors, and it is also pushing to have an investment bank appointed to conduct a “strategic review” of the company.

This past Friday, Clariant management indicated that it had had enough, moving to resist the demands of While Tale. Group chief executive Hariolf Kottmann fears that the investor is seeking to carve up the company and sell it off bit by bit. With positions now so intractable, everything would point to a standoff with While Tale – which has the support of several activist investors – at the coming shareholder meeting in March of next year.

This example serves to illustrate that practices long common in the USA are now to be encountered in Europe ever more frequently. Europe-wide, there has been a sharp rise in the number of activist campaigns – as reflected in the figures collated by information service Activist Insight and other publicly available sources. While, seven years ago, there were just six advances made to companies with a market capitalization of a billion euros or more, in 2016 there were already 40 activists trying their luck. The most spectacular examples to date in the current year have been the campaigns of Petrus Advisors at Commerzbank subsidiary Comdirect, Active Ownership Capital at Schaltbau Holding and at drugmaker Stada, and by Elliott at engineering group Gea. In the coming year, chief executives are likely to come under even greater pressure.

Lots of intersecting and overlapping interests. There is, after all, now a growing willingness on the part of institutional investors such as fund companies and pension funds to support activist investors and to become active themselves, notes Klaus Röhrig, founding partner of Active Ownership Capital. This is borne out by Michael Schmidt, a member of the management board at Deka Investments, one of the biggest fund companies. “There definitely are overlapping interests between activist investors and asset managers such as Deka.” These could, for example, encompass good governance or the overall business strategy. “Both groups want to wield influence in order to enhance the value of their investments," says Schmidt. And Larry Fink, head of BlackRock, the world's largest asset manager, wants to use the activists to his own ends. In the letter that he this year wrote to some 200 of Europe's top companies, he cautioned against disregarding his advice on good governance. Otherwise, he stated, he would be willing to support the plans of "long-term activists" if they offered a better strategy than the management of those companies.

Activist shareholders buy into companies by acquiring a minority stake of three, five, or ten per cent and subsequently demand a restructuring, the replacement of existing management, seats on the supervisory board, or the divestment of company divisions. "Activist hedge funds have hitherto been most frequently encountered in the M&A arena, where they speculate on obtaining higher squeeze-out payments," notes Alexander Mayer, partner at investment bank Goldman Sachs in Germany. "Yet that has since changed, with efforts now being made to exert a direct influence on company policy." Christian von Engelbrechten, fund manager with Fidelity Germany Fund, makes it quite clear that many examples have shown that such investor groups were invested in successful restructurings. For Engelbrechten, such a success was most notably the case with investor Permira, which was instrumental in pushing through the turnaround at fashion group Hugo Boss. The stock prices of the restructured companies have, he points out, increased more than twentyfold when measured against their lows. Yet there are also examples (see panel) of where the opposite has been the case.

Worried CEOs

To avoid exposing any vulnerabilities to activist investors, experts advise chief executives to watch out for three warning signs. First, disappointments on the earnings front, be these the latest figures or forward guidance. Second, management problems or unrest at the executive management level. Third, a poorly performing stock price. Anyone ticking two or three of these boxes is likely to face the threat of a visit from activist investors.

The top executives of many a company here in Germany are therefore now already taking early action to optimize corporate structures. "Increasingly, activist investors are no longer afraid to make approaches to larger German and European companies, the US market having been largely picked clean and their capital needing to be moved on somewhere," says Ingo Speich, fund manager at Union Investment. Investment bankers advise company management on plans to resists such advances, the blueprints for action already generally to hand in a drawer somewhere. Above all, however, what is impressed upon executives by their advisers is that they cannot afford to ignore the specialized hedge funds and need to seek dialogue instead. Listed German companies have thus already changed a lot. "Far more frequently, today's management boards and supervisory boards bear personal liability and are therefore more cautious in their dealings with activists than was previously the case. That, in turn, increases the willingness to listen to activists," says Matthias Horbach of law firm Skadden, Arps, Slate, Meagher & Flom.

At the same time, Dax companies such as retailing giant Metro have broken up their companies or put in place arrangements that enable them to respond quickly. "Conglomerates are undergoing a thorough review. A 'sum-of-the-parts' consideration used to be a theoretical concept, hidden away in the back pages of the research reports. Today, the analysis of individual company units is a highly relevant benchmark for the assessment of diversified companies," says banker Meyer.

That the activists are succeeding is evident from the figures for 2016. Hedge fund TCI, for example, made a return of 13.5 per cent on the capital it deployed in Europe, and at Cevian the figure was as high as 19.4 cent. Several hedge funds pursuing different investment strategies were a long way from equaling this.

STADA
Mobilization

Without activist investor Active Ownership Capital (AOC), pharmaceuticals company Stada would have remained a company earning decent money selling generics and pills such as Grippostad and Ladival – but no more than that. Yet AOC, headed by Klaus Röhrig and Florian Schuhbauer, identified additional earnings opportunities at the company and went into action. The hedge fund took a stake of around five per cent of the equity and set about shaking up the Bad Vilbel-based company, whose shares are listed on Germany's midcap MDax index. After its entry into the company in spring of the past year, the activist investor ousted chief executive Hartmut Retzlaff and supervisory board chairman Martin Abend, after which the company became a takeover target. Several private equity firms tendered bids, with investors Bain and Cinven ultimately sewing up the deal. Others, in addition to Röhrig and Schuhbauer, profiting from the takeover include well-known activist Paul Singer with his hedge fund Elliott. He joined the takeover party by acquiring a stake of 15 percent - and also made a pretty penny on the deal.