



# SCHOOL OF ECONOMICS AND MANAGEMENT

Bachelor Thesis

Department of Economics

May 2024

Supervisor: Claudio Daminato

## **Boardroom Brawls and Stock Surges: The Comedy of Shareholder Activism**

Authors

Ludvig Rippe & Carl Ragnartz

## **Abstract**

This thesis examines the impact of shareholder activism on the annual stock returns of targeted companies. Utilizing a dataset of activist campaigns from the FactSet SharkWatch 50 database, covering the period from 2005 to 2021, we investigate whether the presence of activist investors leads to enhanced stock performance. Our empirical analysis, employing an event study design, reveals a significant positive effect of activist ownership on annual returns, with an average increase of approximately 6.14%. This effect is most pronounced in the year following the announcement year of the activist campaign, showing an increase in returns by around 14.55%. Interestingly, our findings indicate that neither any degree of activism nor board representation by activists significantly leads to excess returns beyond the overall effect of shareholder activism. This suggests that while activist involvement generally boosts stock performance, the specific strategies activists employ may not be the driving factor behind these gains. These results contribute to the broader literature on shareholder activism by providing a more recent perspective on its financial impact and highlighting areas for future research, including the long-term effects of activism and the qualitative aspects of activist strategies.

# Table of Contents

1. Introduction.....	5
1.1 Background.....	5
1.2 Formulation of Research Questions.....	6
1.3 Methodology Overview.....	7
1.4 Preview of Results.....	7
2. Previous Research.....	7
2.1 Institutional Shareholder Activism.....	8
2.1.1 Operational Impact from Institutional Shareholder Activism.....	8
2.1.2 Abnormal Returns from Institutional Shareholder Activism.....	8
2.2 Hedge Fund Activism.....	8
2.2.1 Operational Impact of Hedge Fund Activism.....	9
2.2.2 Abnormal Returns from Hedge Fund Activism.....	9
2.3 Contributions to Previous Literature.....	10
3. Theoretical Framework.....	11
3.1 Capital Asset Pricing Model (CAPM).....	11
3.1.1 Security Market Line.....	11
3.2 Efficient Market Hypothesis (EMH).....	12
4. Institutional Settings.....	13
4.1 Shareholder Activism.....	13
4.2 Activist Tactics.....	14
4.3 Activist Strategies.....	14
4.4 Activist Return Profile.....	15
5. Methodology.....	16
5.1 Study Design.....	16
5.2 Defining Degree of Activism.....	17
5.3 Empirical Specification.....	19

6. Data.....	20
6.1 Activism Campaigns.....	20
6.2 Descriptive Statistics.....	21
7. Result.....	23
8. Discussion.....	26
8.1 Discussion - Previous Literature.....	26
8.2 Discussion - Theoretical Framework.....	27
8.3 Discussion - Suggested Further Research.....	28
8.3.1 Long-Term Effects of Shareholder Activism.....	28
8.3.2 Qualitative Aspects of Activist Strategies.....	28
8.3.3 Board Representation by Activists.....	28
9. Conclusion.....	29
References.....	30

## List of Figures and Tables

### Figures

Figure 1: Event Window.....	16
Figure 2: Scatter Plot - Average Return over Event Study.....	23

### Tables

Table 1: Classification of Campaign Objectives into Degrees of Activism.....	17
Table 2: Descriptive Statistics - Return (Dependent Variable).....	21
Table 3: Descriptive Statistics - Event Study (Explanatory Variable).....	22
Table 4: Descriptive Statistics - Level of Activism (Explanatory Variable).....	22
Table 5: Descriptive Statistics - Activism Board Representation (Explanatory Variable).....	22
Table 6: Regression analysis (1) - Annual Returns Event Time Analysis.....	23
Table 7: Regression analysis (2) - Annual Return Event Period.....	24
Table 8: Regression analysis (3,4,5) - Annual Return, Level of Activism, & Board Representation by Activist.....	25

# 1. Introduction

## 1.1 Background

The rise of shareholder activism can be traced back to the 1980s, characterized by a significant increase in institutional shareholding, particularly from pension and mutual funds that actively influenced the company's management. Ever since, the activism landscape has evolved with changed regulations, resulting in considerable momentum gained in the 21st century. This momentum was primarily driven by the rise of hedge fund activism, reflecting a shift in the types of shareholders pursuing activism agendas (Gillan & Starks, 2007). Today, Shareholder activism is more relevant than ever before. In 2023, the number of campaigns performed by activist shareholders reached a new all-time high (Lazard, 2024). Further, activist hedge funds have seen substantial growth in assets under management (AUM), with the 50 most prominent activist funds managing approximately \$156 billion (Kirman et al, 2024).

The *raison d'être* of shareholder activism and the fundamental reason investors pursue these active ownership agendas is to maximize their returns. Unlike passive shareholders, activists aim to gain influence and directly impact the returns from their investments. These active agendas can manifest in various ways and can be described along a spectrum.

On one end of the spectrum, activism can involve investors actively trading shares based on their evaluation of the company's performance and management decisions. Conversely, at the other end, activism can include attempts to influence corporate control and introduce substantial changes within the corporation. This assertive end of the spectrum often includes hedge funds aiming to achieve board representation in the targeted company to influence corporate governance and managerial decisions (Cloyd, 2015; Barry, 2017).

Once the activists have placed themselves somewhere on the abovementioned spectrum, different strategies to maximize returns could be pursued. These will most commonly center around three main objectives: capital allocation, corporate governance, and operations. Considering capital allocation, M&A is commonly associated with activist ownership, with over 40% of all activist campaigns featuring an M&A-related agenda, according to (Lipton et al. 2024).

Previous research on activism has two main paths: (i) assessing the impact of activism on operational performance and (ii) determining whether the activism agenda has generated abnormal returns. Considering the impact on returns, Brav et al. (2008), Becht et al. (2015), and Denes et al. (2017) analyzed the effect on returns in firms targeted by activist shareholders. They found that shareholder activism generated abnormal returns within their studies' sample periods. Further, Becht et al. (2015) analyzed the most successful type of activism strategy by studying the outcomes of activism campaigns, such as changes in the board, takeovers, or restructuring efforts that historically have generated the highest returns.

Against this background and in light of previous studies concluding that activists and their campaigns manage to generate abnormal returns, our thoughts come down to what factors impact the returns for activist campaigns. Firstly, similar to Brav et al. (2008), we want to present a more recent perspective on the activist's effects on annual stock returns in target companies using a more recent data sample. Further, in line with Becht et al. (2015), we want to take a closer look at the activist role and their strategy as a factor in generating returns. We also examine the effect on the return of having board representation in the targeted company.

## **1.2 Formulation of Research Questions**

The rationale behind our first research question is to give a more recent perspective on whether the involvement of activist investors who push for changes to improve company performance leads to higher annual stock returns for the targeted companies. The research question is formulated as follows:

*Does Activism Ownership Enhance Annual Stock Returns in Targeted Companies?*

Our second research question focuses on the activist's perspective, specifically if a superior activist strategy exists. We do this by defining the degree of activism and considering board representation by activists. The research question is formulated as follows:

*To what extent does the Degree of Activism and Board Representation by Activists Affect Annual Stock Returns in Target Companies?*

### **1.3 Methodology Overview**

Our study entails an empirical analysis of activist campaigns undertaken by leading activist funds worldwide from 2005 to 2021. We source our data from the FactSet SharkWatch 50 screener, which tracks the activities of the top 50 activist funds globally and their corresponding campaigns. To conduct our analysis, we employ an event study research design using panel data, with annual returns of the targeted firms as the dependent variable. First, we estimate the effects of being targeted by an activist fund on annual returns. Second, we examine whether the degree of activism and board representation leads to enhanced annual returns beyond the general effect of activist ownership. After the analysis, we comprehensively interpret and evaluate the findings, situating them within the existing literature and financial theories. Additionally, we offer insights into potential avenues for future research that could lead to valuable findings within the field.

### **1.4 Preview of Results**

Our study finds a significant positive impact of activist ownership on the annual stock returns of targeted companies. Specifically, the presence of activist investors is associated with an increase in annual returns by approximately 6.14%. This effect is particularly pronounced in the year following the activist campaign announcement, with increasing returns of around 14.55%. Interestingly, activists' degree of activism and board representation do not significantly lead to excess returns beyond the overall effect of activist ownership. This suggests that while the involvement of activist investors generally enhances stock performance, the specific strategies activists employ do not influence return outcomes.

## **2. Previous Research**

The research on activism is divided into two main paths: (i) assessing the impact of activism on operational performance and (ii) determining whether the activism agenda has generated abnormal returns. Initially, in line with the development of regulations, most of the early literature on activism focused on institutional funds. As the regulatory landscape evolved, hedge fund activism emerged and shifted the narrative of what characterized activist investors, leading



to a corresponding shift in the research on the subject. Below, we present previous studies on institutional shareholder activism and hedge fund activism within these two research paths.

## **2.1 Institutional Shareholder Activism**

### **2.1.1 Operational Impact from Institutional Shareholder Activism**

Many previous studies have analyzed if institutional shareholder activism enhances operational performance among target companies. Karpoff et al. (1996) and Smith (1996) conclude that institutional activism does not enhance operational performance. However, Denes et al. (2017) refer to research indicating increased operating return on assets in firms targeted by institutional activism compared to other companies. Most research, however, indicates that institutional shareholder activism does not lead to enhanced operational performance in targeted companies.

### **2.1.2 Abnormal Returns from Institutional Shareholder Activism**

Brav et al. (2008) conclude that institutional funds have less incentive than hedge funds to generate excess returns, which is reflected in the returns from the different activist investors. Denes et al. (2017) present a meta-analysis with 38 studies investigating the effects on returns from different types of activism, both short-term event windows around the campaign announcement date and the “long-run returns”. The findings contradict the “short-term” and “long-term” effects and the type of activism. Looking at the institutional shareholders and their effect on long-run returns, the study made by Smith (1996) indicates a statistically significant positive relationship between institutional activism and long-run stock returns.

## **2.2 Hedge Fund Activism**

Most research on hedge fund activism is based on data from the U.S. Securities and Exchange Commission (SEC) and, more specifically, the 13D filings. The document must be filled and submitted within ten days by any investor acquiring 5% or more of the total shares in a company intending to influence the company. For obvious reasons, these filings only reflect transaction activity in the U.S. market. Research on hedge fund activism in other markets is most frequently based on hand-collected samples of hedge funds describing themselves as activists and their respective disclosed positions.

### **2.2.1 Operational Impact of Hedge Fund Activism**

Bebchuk et al. (2015) examined the operational performance of companies targeted by hedge fund activism. The study is based on around 2,000 observations of hedge fund activist interventions from 1994-2007 (US, 13D filings). Their study empirically validated the ongoing debate and claims about hedge fund activism negatively impacting operational performance and shareholder value. The study found no evidence that the claims about the negative impact of hedge fund interventions were valid. Instead, they found that the interventions improved company performance in the long term.

Similar to the abovementioned findings, Brav et al. (2008) also conclude that hedge fund activism improves operational performance in the targeted companies. The study was based on a sample of 13D filings in the US from 2001 to 2006 and defined operational performance in the targeted firms by evaluating growth and ROA (return on assets).

### **2.2.2 Abnormal Returns from Hedge Fund Activism**

The subject of hedge fund activism and its impact on financial markets has attracted significant research interest. Various studies have tried to understand the return outcomes of activist interventions and the factors driving successful campaigns.

Brav et al. (2008) conducted a thorough investigation using data collected manually from 2001 to 2006, focusing on hedge fund activism. They used market indexes as benchmarks, such as the Russell 2000 Value Index, to assess whether target companies experienced abnormal returns during this period. Additionally, to examine the market's reaction to hedge fund activism, they conducted an event study around the announcement dates of activism. Their findings indicated a positive market response to campaign announcements, followed by target firms closely tracking market indexes. This led to abnormal growth in the short term and over the subsequent year.

Similarly, Becht et al. (2015) explored this phenomenon in a more recent study covering 1,740 activist engagements across 23 countries between 2000 and 2010. Like Brav et al. (2008), they employ an event study to examine the market's reaction to activism engagement in an international context as well. Alongside this, they also employ various regressions to examine

the effect of campaigns with specific "outcomes", such as changes in the board, takeovers, or restructuring efforts. They found that activist hedge funds could generate abnormal returns if campaigns had specific outcomes. In contrast, campaigns without such outcomes did not generate abnormal returns during the period.

Kedia et al. (2021) took a different approach, examining the ownership structure within target companies to identify patterns associated with successful activism. They highlighted the importance of cooperation among hedge funds and other institutional investors, particularly those hedge funds with small stakes in targeted firms. Their analysis categorized institutional investors as "activism-friendly" or not, running a logistic regression to examine the likelihood of a firm being targeted by hedge fund activists. Companies with "activism-friendly" ownership led to increased shareholder returns compared to the "non-friendly."

### **2.3 Contributions to Previous Literature**

Brav et al. (2008) which explore the financial returns from hedge fund activism and Becht et al. (2015), which analyze the outcomes of campaigns and their subsequent effects on returns from hedge fund activism, are highly relevant to our study. Similar to previous studies, we employed an event study design to analyze the impact of activist campaigns. Still, unlike Brav et al. (2008) and Becht et al. (2015), which relied heavily on SEC 13D filings for data collection, we utilized the FactSet SharkWatch 50 database. This allowed us to capture a broader and more recent sample of activist campaigns from 2005 to 2021, encompassing a broader geographical scope and focusing on the most prominent activist funds. This approach also allows us to filter out smaller, less influential actors and instead focus on more prominent activist funds.

Additionally, unlike Becht et al. (2015), our study shifts the focus from campaign outcomes to the initial objectives and corresponding degree of activism of these campaigns, as we believe this more accurately reflects overall performance. We also place greater emphasis on board representation and its effects. Furthermore, we contribute to the existing literature by examining a more recent sample of campaigns, providing an updated perspective on the effects on returns from shareholder activism.

### 3. Theoretical Framework

In this section, we explore the financial theories that underpin the relationship between risk and return, as well as other relevant theories that provide a foundation for understanding the empirical results of this thesis. These theories include the Capital Asset Pricing Model (CAPM), Efficient Market Hypothesis (EMH)

#### 3.1 Capital Asset Pricing Model (CAPM)

The Capital Asset Pricing Model (CAPM) is a financial theory that describes the relationship between systematic risk and expected return on assets, particularly stocks (Byström, 2020). The CAPM formula is given by:

$$E(R_i) = R_f + \beta_i(E(R_m) - R_f)$$

Where:

- $E(R_i)$  is the expected return on the capital asset.
- $R_f$  is the risk-free rate.
- $\beta_i$  is the asset's beta, measuring its volatility relative to the market.
- $E(R_m)$  is the expected return on the market
- $(E(R_m) - R_f)$  is the market risk premium

##### 3.1.1 Security Market Line

The Security Market Line (SML) is a graphical representation of the CAPM, showing the relationship between an asset's expected return and its beta. It is a straight line that starts at the risk-free rate and has a slope equal to the market risk premium.

Any asset lying on the SML is considered fairly priced, providing a return proportional to its risk. If an asset lies above the SML, it is considered undervalued, as it offers a higher return for its level of risk. Conversely, an asset below the SML is considered overvalued, offering lower returns for its risk (Byström, 2020).

The main principles of the SML could be highly relevant and applicable to understanding the dynamics of operational changes and their effect on company-specific risks. Thus explaining the value-creation process of an activist intervention.

### **3.2 Efficient Market Hypothesis (EMH)**

In short, the Efficient Market Hypothesis (EMH) assumes that financial markets are “efficient” in reflecting all publicly available information in stock prices (Byström, 2020). Thus, this hypothesis implies that it is impossible to consistently achieve higher-than-average returns through the fundamental selection of stocks, assuming that your stock picking is based on publicly available information. Further, EMH is categorized into three forms: weak, semi-strong, and strong.

- Weak form: All past trading information, such as price and volume, is incorporated into the stock price. This means that technical analysis, in which investors will analyze prior price-and volume movements, is not a consistent investment strategy to outperform the market.
- Semi-strong form: All publicly available information is reflected in the stock price, including all economic- and financial data such as financial statements and news reports. This suggests that the fundamental analysis of a company, which activist investors will conduct, is not consistent with achieving above-average returns.
- Strong form: All information, including non-public (insider) information, is incorporated into the stock price, suggesting that not even corporate insiders can consistently achieve excess returns in the stock market.

Activist investors will challenge the EMH by exploiting company inefficiencies and try to improve the company by trying to find undervalued stocks that have the potential to generate higher-than-average returns for its shareholders. As previously stated, several studies find that hedge fund activists generate positive abnormal returns, which indicates that markets may only fully incorporate the potential value improvements that activists impose after they occur.

## **4. Institutional Settings**

### **4.1 Shareholder Activism**

Shareholder activism ("activism") is a broad term that represents a range of activities by one, or more investors of a publicly traded company that are intended to affect the decision-making in the company (DeNicole, 2021). These investors will fall along a spectrum based on their desired change and assertiveness of the investor's activities. On the more aggressive end of the spectrum is hedge fund activism, which has become an increasingly familiar concept, with activist campaigns steadily increasing over the past 20 years (Cloyd, 2015) and recently reaching all-time high levels, considering the number of campaigns worldwide (Lazard, 2024).

Maximizing returns is one of the most fundamental reasons, also known as generating cumulative abnormal returns (CARs), for why investors engage in shareholder activism. As opposed to passive investing, shareholder activism allows investors to gain influence and more directly impact their investment returns. By acquiring a large block of shares, on average, a stake of circa 11% (Becht et al., 2015) and engaging in a proxy contest to obtain influence over the board (Cloyd, 2015). For a successful proxy contest, the activist investor will use various tactics to ensure they receive board seats represented by a third party or themselves (DeNicola, 2021). After successfully achieving influence over the company, the activist investor will start implementing various strategies to enhance the company's financial returns and, ultimately, the share price.

Furthermore, another purpose for which a hedge fund activist will target a company is to push for changes in corporate governance (DeNicola, 2021). This involves increasing transparency and accountability, usually done by enforcing new policies and removing certain officers. Increasingly, activist investors focus on environmental, social, and governance (ESG) issues, intending to adopt more sustainability and social responsibility in their target companies (DeNicola, 2021). Most notably, one of the largest and most influential activist funds, TCI fund management, has an outspoken ESG policy that they apply to their investments (TCI, 2023).

## **4.2 Activist Tactics**

As briefly discussed, to achieve influence over the board whilst being a minority owner (Becht et al. 2015), the activist investor will use various tactics to persuade other shareholders to vote for them at the annual general meeting to receive board representation. One critical approach is for activists to draft "white papers" with the help of financial advisors, in which they aggressively use public relations techniques to exploit flaws within the company and the current board and how they (the activist investor) can improve the company, and thus increase shareholder value, by deploying various strategies (Lipton et al. 2024). For example, activist investor "Trian Partners" issued a white paper back in March 2024 regarding the upcoming annual general meeting for Disney Corp. in which they openly critique the current board and propose their choice of potential board members to represent them (the activist investor) and how they would change the company (Trian Partners, 2024). Alongside publishing a lengthy report in the form of a white paper, Trian Partners also participated in various forms of public media to announce their intentions and explain why other shareholders should vote for them in the upcoming proxy. However, This specific proxy contest proved unsuccessful as the proposed board members from Trian Partners did not get enough votes to be selected for the board. Thus, the fund can not implement its desired strategies to drive the stock price. This is a common phenomenon, that is, activist investors do not receive a board seat in an activist campaign, which would then be considered unsuccessful. In 2023, only 35.8% of all activist campaigns turned out successful, according to FactSet's recent data. To improve the probability of achieving influence in the company, activist engagements sometimes involve more than one activist hedge fund, which may coordinate formally or informally. This is called a "wolfpack", for which Becht et al. (2015) estimates are associated with almost one-quarter of all engagements and achieve some of the highest returns for shareholders.

## **4.3 Activist Strategies**

To serve its primary purpose, which is maximizing shareholder returns, activist investors will use a specific set of investing strategies once they have obtained an influence over the target company. These will center around three main objectives: capital allocation, corporate governance, and operations. As for capital allocation, activism will usually be oriented around

M&A, with over 40% of all activist campaigns featuring an M&A-related agenda, according to (Lipton et al., 2024). Furthermore, these can be divided into three separate types of M&A activism: firstly, a strategy to sell the entire company; secondly, strategies that focus on breaking up the company by divesting certain assets, for example, a business division; lastly, it is common for activists to attempt to scuttle or improve an existing deal (Lipton et al., 2024). Additionally, these activist investors, on the topic of improving capital allocation, could increase share buybacks to increase short-term stock prices (Lipton et al., 2024). Operationally, to achieve CARs, activist investors will impose several company-specific strategies to improve the cost spending and thus maximize operational efficiency. Usually, this involves cutting headcount and slashing salaries, as with the recent example where hedge fund activist TCI fund management published a report aimed at Alphabet Inc. stating that they need to lower headcount and its salaries to maximize shareholder value as the company is currently paying among the highest salaries in the industry and growing its labor force at an unsustainable pace (TCI, 2023). Activist investors will also analyze the target company more separately and implement company-specific strategies to improve operational efficiency. For example, in 2014, activist investor Starboard Value published a lengthy report detailing operational issues and strategic missteps at Darden Restaurants and, more specifically, its subsidiary Olive Garden. In this report, Starboard Value outlines various proposals on how Darden can improve its cost efficiency by providing company-specific strategies, such as introducing a new one-breadstick-per-person policy to minimize food waste and improve the operational efficiency of each restaurant (Starboard Value, 2014). Regarding enhancing corporate governance in companies, activist investors often restructure the board and sometimes propose leadership changes to change the target company's strategy. Using a previous case study of the hedge fund activist Starboard Value and its engagement in Darden Restaurants, it is possible that the investor also used strategies to improve corporate governance. In this case, Starboard Value successfully replaced the entire board with its slate of nominees (Starboard Value, 2014).

#### **4.4 Activist Return Profile**

Due to the limited access and insight into hedge fund activists' performance, it is difficult to compare the returns of the activist industry to an appropriate benchmark index. The limited access relates to hedge fund activists preferring not to disclose their performance to other



stakeholders than its partners publicly. However, several articles conclude that hedge fund activism often results in significant positive cumulative abnormal returns. These returns are typically seized around the announcement period of the activist's stake in the target company and can persist for several years afterwards.

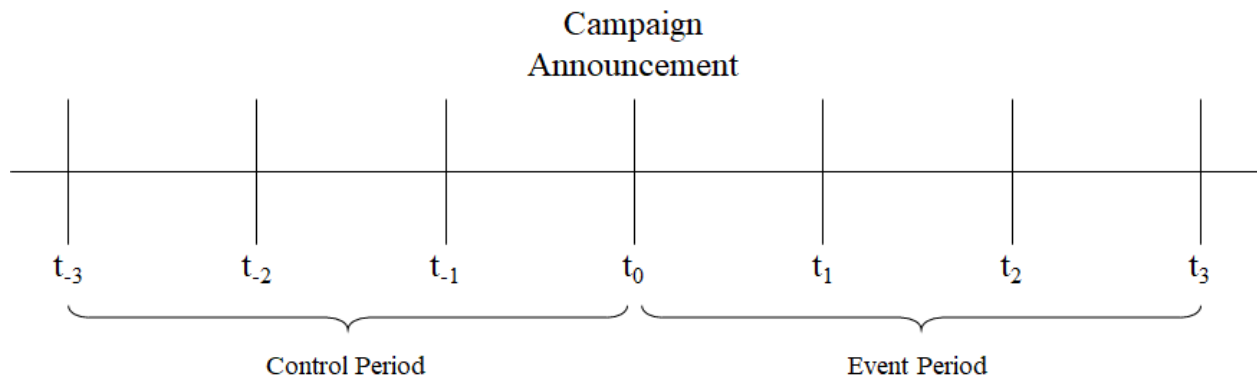
## 5. Methodology

Our analysis centers around empirical studies, where we approach our two main research questions by running different panel data regressions. As we progressed with our analysis, we had to create some new variables and transform some already existing variables. Below, we provide a detailed explanation of our method for conducting this study in chronological order.

### 5.1 Study Design

The first objective is understanding whether shareholder activism enhances annual returns in target companies. To do this, we employ an event study design in which the "event" corresponds to an activist campaign. We then use companies that will be targeted by shareholders later in the sample period as a control group for the companies targeted earlier. We condition on campaign fixed effects to capture unobserved time-invariant company factors that affect returns and the timing of the campaign. We have to create an event window around every campaign ID's respective campaign announcement date. The event window ranged from 3 years before the campaign announcement date to 3 years after, combining 7 annual return observations for each target company.

Figure 1: Event Window



This setup enabled us to capture effects on the annual return depending on the time of the campaign announcement date. This event window was also necessary to correctly interpret the effects on return from different degrees of activism and board representation by activists.

## 5.2 Defining Degree of Activism

For the campaign objective variable, we have classified the level of activism on a scale from 1 to 5 based on the objective characteristics. A rating of 1 represents the least aggressive activism strategy, while a rating of 5 signifies the most aggressive activism. To classify the campaign objectives, we ranked them based on common industry practices, according to practitioners in the industry. In Table 1, we present the methodology and motivation behind the transformation of initial campaign objectives into degrees of activism;

**Table 1: Classification of Campaign Objectives into Degrees of Activism**

Score	Campaign Objective	Motivation
1	13D Filer – No Publicly Disclosed Activism	Involves a significant investment (>5% ownership stake) but no direct attempt to pursue investor activism.
1	Vote For a Management Proposal/Support Management	This aligns with the existing management’s proposal and can be achieved without significant influence. Thus showing minimal activist agenda.
2	Vote For a Stockholder Proposal	Considered to be active but not confrontational. Supporting other shareholders' agendas is assumed to be a passive form of activism.
2	Enhance Corporate Governance	Nowadays, a more common practice as most institutional investors will try to influence and contribute with proposals regarding ESG.
3	Maximize Shareholder Value	This is a broad term that most public investors will try to pursue in the hunt for returns. In an activist context, however, this involves pushing for strategies to increase the stock price, such as improving the internal capital allocation and/or operational efficiency.
3	Vote Against a Management Proposal	Confrontational and potentially influencing corporate governance, but without seeking control.

3	Seat(s) Granted – No Publicly Disclosed Activism	Gaining board seats quietly, without any public activism, suggests a substantial influence that could potentially become more aggressive.
4	Vote/Activism Against a Merger	Similar to voting against a management proposal as it involves confrontation of current strategy and non-alignment with the management. Could impose a significant impact on the decision-making, depending on the size of the proposed merger.
4	Support Dissident Group in Proxy Fight	Indicates a higher degree of confrontation as it involves taking sides with an opposing group to fight the current management, which is considered to be a high degree of activism.
4	Board representation	Seeking direct representation on the board, with the intent to influence the company’s decision-making, reflects a high level of investor activism.
4	Remove officer(s)	Involves a high degree of confrontation as it expresses mistrust and is only possible with major influence.
5	Remove Director(s), No Dissident Nominee to Fill Vacancy	Aiming to remove directors is perceived as a high level of activism, much like removing officer(s). Considered to be more aggressive in the case of no dissident nominee to fill a vacancy as it disrupts the current governance structure.
5	Public Short Position/Bear Raid	Publicly betting against a company is seen as a direct attack on the company’s perceived value and the performance of management. Thus, it can be highly disruptive.
5	Board Control	Allows for the investor to decide on significant changes for the company. Assumes a majority on the board being represented by the activist investor.
5	Hostile/Unsolicited Acquisition	Bidding to take over the control of the company without any prior consent from the current management is the most aggressive form of activism.

*Note: The table provides an explanation and motivation for classifying the “campaign objective” into degrees of activism.*

### 5.3 Empirical Specification

The event study design leads us to the following event-study specification to estimate the effect on the annual return of the activist campaign:

$$(1) \quad R_{i,t} = \alpha_i + \sum_{e=-3}^3 \beta_e \text{Event\_Time}_{i(t+e)} + \epsilon_{i,t}$$

Our dependent variable  $R_{i,t}$  represents the annual return for firm  $i$  in year  $t$ . For our explanatory variables, we have a dummy variable for each of the years included in the event window (except omitted,  $e = -1$ ).  $\text{Event\_Time-3}$  represents three years before the campaign, and  $\text{Event\_Time3}$  represents three years after. The campaign announcement year is  $\text{Event\_Time0}$ , with the intervening years represented sequentially in  $\text{Event\_Time-2}$ ,  $\text{Event\_Time-1}$ ,  $\text{Event\_Time1}$ , and  $\text{Event\_Time2}$ .

Second, we analyzed the overall effects on the returns of the campaign. In other words, the effect on returns in the periods following the activist's entry point in the target company. To do this, we estimate the following specification:

$$(2) \quad R_{i,t} = \alpha_i + \beta \text{Event\_Period}_{i,t} + \epsilon_{i,t}$$

Our dependent variable  $R_{i,t}$  represents the annual return for firm  $i$  in year  $t$ . Our only explanatory variable,  $\text{Event\_Period}_{i,t}$ , is a dummy variable, taking the value one for firm  $i$  in the period following the activist's campaign announcement and zero for the period before.

Next, we want to examine whether the degree of activism performed by activists or if board representation by activists affected the returns in the target companies. To do this, we created some interaction variables as we still had to consider the timing aspect relative to the campaign announcement. Firstly, we generated dummy variables for every level of activism ( $\text{Level\_Activism1}, \dots, \text{Level\_Activism5}$ ). We generated interaction (Named:  $\text{Interaction1}, \dots,$

*Interaction5*) between *Level\_Activism* 'i' for every *i* and *Event\_Period*. The estimated model is as follows:

$$(3) \quad R_{i,t} = \alpha_i + \beta_1 Interaction2_{i,t} + \beta_2 Interaction3_{i,t} + \beta_3 Interaction4_{i,t} + \beta_4 Interaction5_{i,t} + \beta_5 Event\_Period_{i,t} + \epsilon_{i,t}$$

Further, we generated a new variable *highactivism* by grouping the highest levels of activism, 4 & 5, into one variable. Like the interaction variables above, we generated a new interaction variable called *highact\_event* between the variables *highactivism* & *Event\_Period*. We then regressed the following model:

$$(4) \quad R_{i,t} = \alpha_i + \beta_1 highact\_event_{i,t} + \beta_2 Event\_Period_{i,t} + \epsilon_{i,t}$$

Lastly, we wanted to analyze if activist board representation affected annual returns. Like the method above, we generated a variable, *board\_event*, between the variables *ActivismBoardRepresentation* & *Event\_Period*. The estimated model is as follows:

$$(5) \quad R_{i,t} = \alpha_i + \beta_1 board\_event_{i,t} + \beta_2 Event\_Period_{i,t} + \epsilon_{i,t}$$

## 6. Data

In this section, we describe the data utilized for our study. This chapter is structured into two main sections: Activism Campaigns and Descriptive Statistics, which provide a comprehensive overview of the data sources, collection methods, and statistical summaries.

### 6.1 Activism Campaigns

We used the FactSet SharkWatch 50 database to extract data for our analysis. The SharkWatch 50 database tracks the most prominent activist funds in the world chosen by FactSet corporate activist specialists. In the database, one can find information about all activist campaigns

involving any of the 50 activist funds in the SharkWatch 50. The data used in our analysis contains campaigns with announcement dates ranging from 2008-2018. However, as we wanted to create an event window ranging from 3 years before the announcement of the campaign to 3 years after, we gathered the annual return (dependent variable) excluding dividends from each targeted company for every year within their respective event window, increasing the sample period to 2005-2021. For each campaign and year corresponding to their respective event window, we also downloaded the campaign-specific information of “Campaign Objective” and “Board Representation by Activist” (explanatory variables) using FactSet. We drop all campaigns with missing values for any variable in their respective event window. Following this process, we had 738 unique campaigns and 5,166 total observations.

Considering our explanatory variables, we obtained information about the objective of our remaining sample of 738 campaigns. More specifically, this is expressed as a sentence explaining the primary intention, from the activist point of view, of the campaign at the time of the campaign announcement date. Further, our following explanatory variable, named “Board Representation by Activist”, returned the value “1” if the activist had board seat(s) in the targeted company and “0” if the activist had no board representation.

In contrast to earlier research, our different approach to selecting activist funds is most notable. Using FactSet SharkWatch 50, we broadened the geographical scope and narrowed the selection of activist funds. This approach allows us to filter out smaller, less influential actors and instead focus on more prominent activist funds.

## 6.2 Descriptive Statistics

We finally ended up with 5,166 observations ranging from 2005 to 2021. Below, we present some descriptive statistics for the relevant variables.

**Table 2: Descriptive Statistics - Return (Dependent Variable)**

Variable	Obs	Mean	Std. dev.	Min	Max
Return	5,166	9.368109	65.61456	-98.90402	2,508

**Table 3: Descriptive Statistics - Event Study (Explanatory Variable)**

<b>Event Study</b>	<b>Freq.</b>	<b>Percent</b>	<b>Cum.</b>
-3	738	14.29	14.29
-2	738	14.29	28.57
-1	738	14.29	42.86
0	738	14.29	57.14
1	738	14.29	71.43
2	738	14.29	85.71
3	738	14.29	100.00
Total	5,166	100.00	

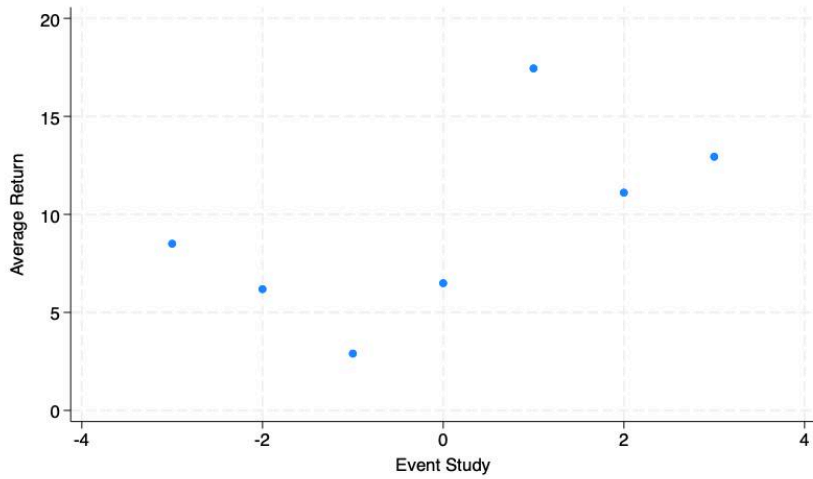
**Table 4: Descriptive Statistics - Level of Activism (Explanatory Variable)**

<b>Level of Activism</b>	<b>Freq.</b>	<b>Percent</b>	<b>Cum.</b>
0	2,214	42.86	42.86
1	404	7.82	50.68
2	256	4.96	55.63
3	812	15.72	71.35
4	1,288	24.93	96.28
5	192	3.72	100.00
Total	5,166	100.00	

**Table 5: Descriptive Statistics - Activism Board Representation (Explanatory Variable)**

<b>Activism Board Representation</b>	<b>Freq.</b>	<b>Percent</b>	<b>Cum.</b>
0	4,278	82.81	82.81
1	888	17.19	100.00
Total	5,166	100.00	

**Figure 2: Scatter Plot - Average Return over Event Study**



## 7. Result

In this section, we will present the results from our different regressions. Similar to the order in the method section, we start presenting an extensive regression, analyzing every year of the event window and the corresponding effects on annual returns. Later, we start presenting the more "high-level" findings on activist ownership and its impact on annual returns in targeted companies. Continuing with heterogeneity analysis, we present our findings about the effect of the activism level performed by the activist on the targeted firms' annual returns. Lastly, we present our results on the effects on targeted firms' annual returns by board representation by activist shareholders. (The number in the table rubric indicates the corresponding model specification in the previous section)

**Table 6: Regression analysis (1) - Annual Returns Event Time Analysis**

R	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
Event_Time-3	5.605	3.447	1.63	.104	-1.153	12.364	
Event_Time-2	3.289	3.447	0.95	.34	-3.469	10.048	
Event_Time0	3.594	3.447	1.04	.297	-3.165	10.352	
Event_Time1	14.55	3.447	4.22	0	7.791	21.308	***
Event_Time2	8.212	3.447	2.38	.017	1.453	14.97	**
Event_Time3	10.044	3.447	2.91	.004	3.285	16.802	***
Constant	2.898	2.438	1.19	.235	-1.881	7.677	

Number of obs

5166



This regression analysis explored the impact of different event stages within the event window. (Defined in the methodology section (Figure 1)). A total of 7 dummies represent each year within the event window, starting from 3 years before the announcement date and continuing 3 years after the announcement year. (*Event\_Time0* represents the campaign announcement year).

*Event\_Time-3* and *Event\_Time-2* do not show statistically significant effects, as indicated by their p-values (0.104 and 0.340). This suggests that the parallel trend assumption holds in these settings.

*Event\_Time0* does not show statistically significant effects on the annual return, reflected by the p-value of 0.297. Suggesting no initial impact on annual returns within the campaign announcement year.

*Event\_Time1* shows a significant positive effect with a coefficient of 14.55, which is statistically significant at the 0.000 level ( $p < 0.001$ ). This suggests an increase of approximately 14.55 units in the annual return 1 year after the campaign announcement date, compared to the baseline (the year before the campaign announcement).

*Event\_Time2* and *Event\_Time3* also show significant positive effects with coefficients of 8.212 and 10.044, respectively, and p-values of 0.017 and 0.004.

**Table 7: Regression analysis (2) - Annual Return Event Period**

R	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
Event_period	6.135	1.863	3.29	.001	2.481	9.788	***
Constant	5.863	1.409	4.16	0	3.101	8.624	***
Number of obs					5166		

The regression analysis was conducted to examine the impact of the campaign, in other words, the impact of activism ownership, on the annual return. The results indicate a significant effect of the event period on the dependent variable. The coefficient for the event period is 6.135, which is statistically significant at the 0.001 level ( $t = 3.29$ ,  $p = 0.001$ ). This suggests that activist ownership increases the annual return by approximately 6.14 percentage points.

**Table 8: Regression analysis (3,4,5) - Annual Return, Level of Activism, & Board Representation by Activist**

<b>Panel A:</b>							
R	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
interaction2	.072	8.091	0.01	.993	-15.79	15.934	
interaction3	2.766	6.166	0.45	.654	-9.323	14.856	
interaction4	2.439	5.775	0.42	.673	-8.884	13.761	
interaction5	7.598	8.878	0.86	.392	-9.807	25.004	
Event_period	3.809	5.039	0.76	.45	-6.07	13.688	
Constant	5.863	1.409	4.16	0	3.1	8.625	***
Number of obs					5166		
<b>Panel B:</b>							
R	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
highact_event	1.569	3.727	0.42	.674	-5.738	8.877	
Event_period	5.348	2.639	2.03	.043	.174	10.522	**
Constant	5.863	1.409	4.16	0	3.101	8.624	***
Number of obs					5166		
<b>Panel C:</b>							
R	Coef.	St.Err.	t-value	p-value	[95% Conf	Interval]	Sig
board_event	-5.086	4.063	-1.25	.211	-13.051	2.88	
Event_period	7.665	2.228	3.44	.001	3.296	12.033	***
Constant	5.863	1.409	4.16	0	3.101	8.624	***
Number of obs					5166		

Panel A analyzes the effects of different levels of activism on the annual return. Interestingly, the results indicate no significant excess returns from different levels of activism compared to activism involvement in general, as p-values far exceed the significance level of 0.05.

Panel B examines the effects of high-degree activism, defined as level 4 & 5 activism, on the annual return. The coefficient for high activism is 1.569, which is not statistically significant ( $p = 0.674$ ). This indicates that high degrees of activism do not have a statistically significant effect on excess returns beyond the overall effect of activism.

Panel C suggests that the event period significantly impacts the dependent variable, implying that the annual return tends to increase during this period. However, once again, similar to the results from Panel A and B, board representation doesn't have a statistically significant effect on excess activism returns, reflected by the p-value of 0.211.

## **8. Discussion**

In this section, we comprehensively analyze and discuss the various findings presented in the previous chapter. We situate the results within the existing literature and theoretical framework presented in chapters 2 and 3. Furthermore, we provide our thoughts on what research within the field of activism could be of interest in the future.

### **8.1 Discussion - Previous Literature**

Our research indicates a significant positive impact of activist ownership on the annual stock returns of targeted companies. Specifically, our findings show an average increase of approximately 6.14% in annual returns, particularly notable in the year following the campaign announcement, with an increase of around 14.55%. This result supports the findings of previous studies by Brav et al. (2008), Becht et al. (2015), and Denes et al. (2017), all of which reported increased returns in firms targeted by activist shareholders. Furthermore, Denes et al. (2017) conducted a meta-analysis of 38 studies on shareholder activism and confirmed that activism generally leads to positive abnormal returns. Our findings align with this broader body of evidence, repeating that activist investors play a crucial role in enhancing shareholder value through their interventions.

Our study provides new insights into the degree of activism and board representation by activists, contrasting with some earlier research findings. Our results indicate that neither the degree of activism nor board representation significantly leads to excess returns compared to the general effect of activist ownership. This finding diverges from studies like Becht et al. (2015), which suggested that specific outcomes of activism campaigns, such as changes in the board, contribute to higher returns. Our results indicate that while activist campaigns generally enhance stock performance, the specific strategies are of minor importance. Our methodology diverges from that of Becht et al. (2015) by focusing on the initial campaign objectives rather than the actual outcomes. This distinction may account for the differences in our results. Activists who achieve their objectives could be more likely to experience higher returns, whereas those who do not achieve their objectives may experience lower returns.

This result could also be interpreted as partly aligned with the mixed evidence in the literature regarding the operational impact of activism. Karpoff et al. (1996) and Smith (1996) found limited improvements in operational performance resulting from institutional activism. This suggests once again that the specific strategies are of minor importance compared to the presence of an activist investor.

## **8.2 Discussion - Theoretical Framework**

As previously mentioned, the CAPM posits that the expected return on an asset is a function of its beta (systematic risk). Our results of a significant positive effect on returns from activist ownership, particularly in the first year following the campaign announcement year, imply that the activist shareholder reduces the systematic risk within the targeted firms. However, our study does not examine the effects on the target companies' risk profile. Thus, we can not say whether our results perfectly align with the CAPM theory, but one can indirectly conclude. Another way of interpreting our results within the framework of CAPM is by considering the security market line (SML). One could think of activists as better than average investors in finding companies placed above the SML, which is considered undervalued as their risk profile is not proportional to its expected return.

Considering the Efficient Market Hypothesis (EMH), our study gives a mixed picture. On the one hand, the noticeably increasing returns after activist actions suggest that markets only fully capture the potential improvements these activists bring once they occur. This points to a semi-strong form of market inefficiency where the market reacts to new, positive information only after it is announced. Conversely, the level of activism and having activists on the board do not significantly affect annual returns, which can be seen as supporting the EMH. This implies that while the market quickly recognises and rewards the presence of activists, the specific strategies they use do not lead to ongoing increasing returns.

## **8.3 Discussion - Suggested Further Research**

The findings from our study on the impact of shareholder activism on annual stock returns open several avenues for further research. This section outlines potential research areas that could expand our understanding of shareholder activism.

### **8.3.1 Long-Term Effects of Shareholder Activism**

While our study identified significant short-term returns following activist campaigns, the sustainability of these returns remains an open question. Future research could investigate the long-term impact of activism on stock performance beyond the three-year event window used in our study. This would involve analyzing whether the initial gains are sustained, increased, or dissipated over a more extended period, such as five to ten years.

### **8.3.2 Qualitative Aspects of Activist Strategies**

Our study quantified the degree of activism and its impact on returns but did not delve into the qualitative aspects of activist strategies. Future studies could conduct case studies of specific activist campaigns to understand the tactical decisions and operational changes implemented. Such research could involve interviews with key stakeholders, including activists, company executives, and board members, to gather insights into the decision-making processes and challenges faced during activist interventions. By examining the qualitative details of successful and unsuccessful campaigns, researchers could identify best practices and common pitfalls, providing practical guidelines for future activists and companies facing activist pressure.

### **8.3.3 Board Representation by Activists**

Our findings indicate that activist board representation does not significantly lead to excess return compared to the general effect of activism. However, this result could be subject to further exploration. Future research could investigate the conditions under which board representation might be more or less effective. For instance, studies could examine the characteristics of activist board members, such as their experience, industry expertise, and network connections, to determine how these factors influence their ability to drive positive changes.

## **9. Conclusion**

This thesis explores the impact of shareholder activism on the annual stock returns of targeted companies, using data from the FactSet SharkWatch 50 database spanning 2005 to 2021. Our findings demonstrate a significant positive effect of activist ownership on stock performance, with an average increase of approximately 6.14% in annual returns. This effect is particularly pronounced in the first year following the activist campaign announcement year, showing an increase of around 14.55%. These results align well with previous research, indicating that activist investors can enhance shareholder value through their interventions. However, our analysis reveals that neither any degree of activism nor board representation by activists significantly leads to excess returns beyond the general activist ownership effect. This suggests that the presence of activist investors may drive performance improvements rather than specific strategies employed by them. This study contributes to the broader literature on shareholder activism, emphasizing the beneficial effects of activism on stock returns while pointing out the need for further research into the qualitative aspects of activist strategies. Future research should focus on case studies of activist interventions to deepen the understanding of what creates a successful activist campaign.

## References

- Barry, N. (2017). Hedge Fund Activism: A Review of Wealth Creation, Operational Efficiency and Corporate Strategy in Targeted Firms
- Bebchuk, L., Brav, A., & Jiang, W. (2015). The Long-term Effects on Hedge Fund Activism
- Becht, M., Franks, J., Grant, J., & Wagner, H. F. (2015). The Returns to Hedge Fund Activism: An International Study
- Brav, A., Jiang, W., Partnoy, T., & Randall, T. (2008). Hedge Fund Activism, Corporate Governance, and Firm Performance. *The Journal of Finance*, Issue 4, pp. 1729-1775.
- Brav, A., Jiang, W., Partnoy, T., & Randall, T. (2008). The Returns to Hedge Fund Activism
- Byström, H. (2020). *Finance*, 4th edn, Lund: Studentlitteratur. pp.187-200, 211-217.
- Castañón, M. (2021). The Director's Guide to Shareholder Activism  
<https://corpgov.law.harvard.edu/2021/06/11/the-directors-guide-to-shareholder-activism/>  
[assessed on 20 May 2024]
- Cloyd, M. (2015). Shareholder Activism: Who, What, When, and How?,  
<https://corpgov.law.harvard.edu/2015/04/07/shareholder-activism-who-what-when-and-how/>  
[accessed on 9 May 2024]
- Denes, M., Karpoff, J., & McWilliams, V. (2017). Thirty years of shareholder activism: A survey of empirical research. *Journal of Corporate Finance*, Issue 44, pp. 405-424
- Gillan, S., & Starks, L. T. (2007). The Evolution of Shareholder Activism in the United States. *Journal of Applied Corporate Finance*, Issue 19, pp. 55-73.

Karpoff, J, Malatesta, P. & Walkling, R. (1996). Corporate governance and shareholder initiatives: Empirical evidence

Kedia, S., Starks., L, Wang. X. (2021). Institutional Investors and Hedge Fund Activism

Kirman, I, Tetelbaum, E, Goldfeld, V. (2024). M&A Developments: Hedge Fund Activism

Lazard. (2024). Annual Review of Shareholder Activism 2023, <https://www.lazard.com/research-insights/annual-review-of-shareholder-activism-2023/> [accessed on 21 May 2024]

Lipton, Katz, Rosen & Wachtell., (2024). Corporate Law and Practice

Smith, M (1996). Shareholder activism by institutional investors: Evidence from CalPERS

Starboard Value. (2014). Transforming Darden Restaurants

TCI Fund Management. (2023). ESG Investment Policy, <https://www.tcifund.com/ESG> [accessed on 12 May 2024]

TCI Fund Management. (2023). 20th of January 2023

Triun Partners. (2024). Restore the magic at the Walt Disney Company