

ACCOUNTABILITY AND TRANSPARENCY

Are Your Corporate Governance Practices Putting You at Risk?

Preparing Your Board to Deal With Activist Shareholders

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ACTIVISM – THE NEW WORLD ORDER

November 6, 2014

Activism – The New World Order

- “Activism” no longer a four letter word.
 - Pension Funds and other historically passive, long term holders have teamed with or supported activists.
 - Voting transparency requirements for mutual funds has forced thoughtful consideration vs. blind adherence to proxy advisory firms.
- “Activism” is now synonymous with:
 - Significant shareholder return.
 - Significant management change.
 - Significant governance change.
 - Significant realignment of corporate and social values.

Emotional Preparedness

- It starts with the demand.
- Remember, shareholders believe you work for them.
- Demonstrate a willingness to listen.
- Take the high ground until you can't.
- Don't be too proud to accept change.
 - Adopting changes during campaigns undercuts activist themes.
 - If the demand is corporate governance change / consider adoption.
 - If Board representation is requested, consider Board expansion and single seat. (Activists can be greedy...use it: Oshkosh.)
- Avoid sound bytes ... bad ones may define your company throughout the campaign.

Strategic Preparedness

- Work from the Activist playbook.
 - Recruit their team / Consider retaining proxy solicitor and PR Firm that have advised activists.
- Know your Shareholders
 - Study their themes and strategies (perform a regular review of activist trends).
 - Keep your friends close and your enemies closer.
 - Identify shareholder base that have demonstrated activist support and establish better / enhanced communication.
- Continue to do what you do best.
 - Focus on performance.
 - Focus on transparency / avoid surprises.
 - Have a strong, diverse Board.

War Stories / “What Were They Thinking”

- Warren Buffet takes control of Berkshire Hathaway / \$.12 cost CEO his job.
- Malan Realty Investors/refusal to meet led to removal of all directors.
- Tech Team International / Board call gone bad led to majority control.
- Orrstown Financial / restrictive by-law amendment in response to 13d filing led to litigation and proxy campaign.
- Central Bancorp / false 13d “group” allegation led to triggering poison pill and multi-million dollar litigation.

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Activism Overview

November 6, 2014



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2014 Activism Highlights

Larger Companies Under Attack



Triam Partners



Triam Partners



Carl Icahn



Carl Icahn



Elliott Management

Contests for Control



Corvex/Related



Casablanca



Starboard Value LP



Glenview Capital Management



TPG-Axon

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Trends & Highlights

Bidder / Activist Joint Ventures



Pershing Square /
Valeant Pharmaceuticals

Special Meetings



Pershing Square /
Valeant Pharmaceuticals



Starboard Value LP

Contested Mergers



Alan Spachman



Brandes Investment
Partners



TIG Advisors

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Trends in Shareholder Activism

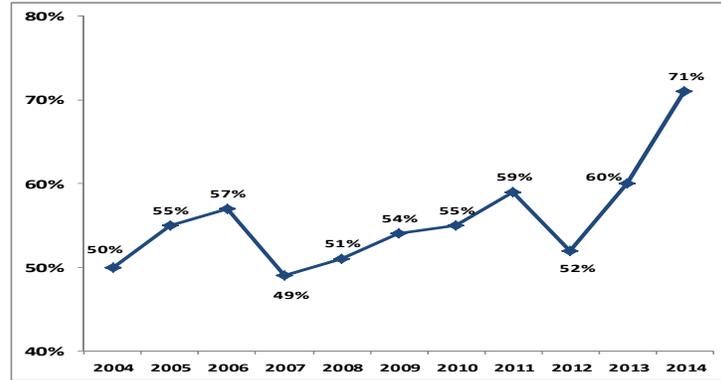
- Growth of dedicated activist funds
 - Publicly traded activist funds
- Increasing diversity of activists
 - Dedicated activist funds
 - Occasional / opportunistic activists
 - Small holder activism
- Accelerating the pace of activism
 - Companies being targeted after short periods of underperformance
 - Activists using special meetings / other tactics to pursue campaigns outside annual meeting window
 - "Real time" activism via CNN, Twitter, etc.
- Recurrent activism
 - Companies can no longer count on being a one-time target

Activist hedge fund assets under management
\$36B in 2009 → \$100B+ in 2014

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Dissident Success in Proxy Contests

Dissident Success Rate¹



¹Number of outright victories, partial victories or settlements by the dissident as a percentage of all proxy contests where an outcome has been reached, as of July 14, 2014

²Includes proxy contests from January 1, 2012 to July 31, 2014, excluding funds

Source: FactSet Shark Repellent

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Key Motivations for Shareholder Activism

Short-Term Gain

Most shareholder activism is motivated by a single goal – to make money, in a timeframe generally measured from a matter of months to 1-2 years

Long-Term Frustration

A substantial, long-term investor or group that is disappointed by investment performance pursues activism, usually as a last resort

Internal Division

A founder, current or former senior manager or board member disagrees with the company's strategy or leadership and campaigns for change

Source: FactSet Shark Repellent

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The Typical Campaign Seeks Short-Term Financial Gain

- In most campaigns the primary driver is not a specific strategy
- Usually multiple investment thesis
 - Some of these will prove flawed
 - Others are outside activist's control – e.g. sale of the company requires a willing buyer
- Many activists constantly change the menu options
 - "Whatever works" – every value creation strategy is a means to an end – drive price improvement and liquidity
 - Activists expect that the target will eventually choose something from the menu – or face a fight

Source: FactSet Shark Repellent

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Types of Activist Campaigns (2012 – 2014)

M&A – Potential M&A Target

Sell Company

- Oshkosh Corp. / Carl Icahn
- BMC Software / Elliott
- Compuware / Elliott
- Gardner Denver / ValueAct

Merger Consideration Insufficient

- National Interstate / Alan Spachman
- Zale Corporation / TIG Advisors
- AsiaInfo Linkage / Brandes Investment Partners

Unsolicited Offer for Company

- Riverbed / Elliott
- Allergan / Pershing Square / Valeant Pharmaceuticals
- CVR Energy / Carl Icahn

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Types of Activist Campaigns (2012 – 2014)

Operational – Underperforming Companies

Change in Management / Board / Structure

- Procter & Gamble / Pershing Square
- Yahoo! / Third Point
- Forest Labs / Carl Icahn
- Darden / Starboard Value LP
- Sotheby's / Third Point
- Hess / Elliott

Change in Operations / Business Strategy

- Stillwater / Clinton Group
- Progress Software / Starboard
- AOL / Starboard
- Oshkosh Corp. / Carl Icahn
- Cliffs Natural Resources / Casablanca
- Mondelez International / Trian Partners

Divest or Spin Assets

- Yahoo / Starboard Value LP
- Dupont / Trian Partners
- Dow Chemical / Third Point
- Darden Restaurants / Barington Capital
- PepsiCo / Trian Partners

Capital Allocation – Balance Sheet Capacity / Cash Rich Situations

Return Cash to Shareholders

- Transocean / Carl Icahn
- Apple / David Einhorn / Carl Icahn
- Microsoft / ValueAct Capital
- Juniper Networks / Elliott
- NetApp / Elliott

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Evolution of an Activist Campaign



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Activist “Playbook”

Build Stake

- Background research to gather information and develop investment thesis (may include “qualification” call/meeting with target)
- Accumulate initial stake (may include use of derivatives to leverage position/avoid regulatory filings)
- Build stake
- File Schedule 13D
- Encourage other hedge funds to enter stock
- Form committee/alliance with other shareholders

Apply Pressure

- Write letters to the company
- Engage/criticize management on earnings call
- Lead ideas to research analyst community and media
- Submit shareholder proposal/agitate for removal of takeover defenses
- Demand company pursue value creation agenda (use of “white papers” to detail thesis)
- Public relations initiative to change board and/or management
- Commence litigation against company

Initiate Proxy Contest/Force Value Maximization Process

- Demand seat(s) on board
- Public recommendation to target to hire an advisor and commence a process
- Hire financial advisor
- Solicit buyers for all or part of business
- “Stalking horse bids”
- Public offer to buy company
- Generally intended to prime a sales process

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Managing Your Investors

Three critical pro-active steps:

Identify Shareholders

- Know who your shareholders are
- Know which investors are likely to support management
- Know the identity of investment and proxy decision makers

Monitor

- Know who is buying and selling your shares
- Know who are the traders vs. owners
- Know how activists purchase shares

Communicate

- Know that activists are likely speaking with your investors
- Know the concerns of your investors
- Make sure that you are communicating your story to your investors

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Top 10 “Do’s” for Staying Prepared

- 1) Be proactive – identify and address potential vulnerabilities
- 2) Keep the board informed and constructively engaged
- 3) Define core messages / positioning and set clear benchmarks
- 4) Keep shareholders close – be nimble and adjust approach as needed
- 5) Engage the dissident
- 6) Take the high road – focus on your company’s strengths and business
- 7) Maintain tight team communications
- 8) Be measured in responses and prepared for rapid response escalation
- 9) Consistently review board composition
- 10) Recognize that everything you say can and will be used against you

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Potential Steps to Avoid Becoming an Activist Target

While every situation is different, there are a number of guidelines for reducing activist vulnerability. Advance preparation is key to successful defense outcomes.

Assess Performance Against Peers

- Review share price performance and operational benchmarking compared to peers
- Assess any potential valuation gaps

Review Capital Allocation Policies

- Comparison of cash balance compared to peers – communication to street on liquidity needs
- Periodic review of potential for changes to buyback or dividend policy
- Provide investor roadmap on capital allocation targets

Review of Business Portfolio

- Review of potential underperforming business units or businesses frequently considered “non-core” by street
- Communications with street on turnaround plans and timing
- Periodic review of potential value creation from asset sales or spins

Investor Communication

- Be mindful of investor sentiment regarding potential “hot button” issues
- Careful communication around acquisition strategy

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Who are the Activists?

- | | | | |
|---|---|---|--|
| <ul style="list-style-type: none">• 3G Capital Partners• Altai Capital• Appaloosa• Atticus Capital• Barington Capital• Becker Drapkin Management• Biglari Capital• Blue Harbour Group• Breeden Partners• Bulldog Investors• Cannell Capital• Carlson Capital• Casablanca Capital• Chapman Capital• Clinton Group• Coghill Capital• Coppersmith Capital• Corvex Management• Crescendo Partners• Davis Selected Advisers• D.E. Shaw & Co.• Dialectic Capital• Discovery Group | <ul style="list-style-type: none">• Dolphin Partners• Elliott Associates• Engaged Capital• Engine Capital• ESL Partners• Farallon Capital Management• First Manhattan• Franklin Mutual Advisers• FrontFour Capital Group• GAMCO• Glenview Capital• Greenlight• Highfields• Highland Capital Management• Icahn Capital• JANA Partners• JCP Investments• Jewelcor Management• Karpus Investment Management• Lawndale Capital Management• Lone Star Value Management | <ul style="list-style-type: none">• Locksmith Capital Management• Loeb Capital Management• Marcato Capital Management• Mason Capital• MCM Management• Mercury Real Estate Advisors• Millennium Management• MMI Investments• Newcastle Partners• Noonday Asset Management• Oliver Press• Owl Spring Asset Management• Pardus Capital Management• Pershing Square• Philip Goldstein• PL Capital• Raging Capital• Red Mountain Capital• Sachem Head• Sandell Asset Management• Sarissa Capital• Scepter Holdings• Seidman and Associates | <ul style="list-style-type: none">• Seneca Capital• SMP Asset Management• Soroban Capital• Stadium Capital• Starboard Value (formerly Ramius)• Steel Partners• Stilwell Value• Third Point• TCI• TPG-Axon• Trian• ValueAct Capital• Voce Capital• Western Investment• Wynnefield Capital |
|---|---|---|--|

...but many others pile on

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