



Activist Insight

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ACTIVISM IN GERMANY

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Activist Insight

Activism in Germany

Activism in Germany has increased over the past two years but is still in a nascent phase. A host of positive developments could accelerate activity in the future.

Germany has always been a difficult space for activist investors, with many choosing not to confront its legal and cultural roadblocks, including two-tiered boards and the disproportionate influence of company founders and their families in equity markets. Over the years, activists that were courageous enough to target German companies were often ostracized by hostile local media and analysts.

Yet despite all the headwinds, 2017 is on track to be a record year for activism, with 16 companies already targeted by the end of September. By comparison, activists advanced public demands at 16 companies in 2016 and 15 companies in 2013, the years holding the previous records.

In a development pointing to the increased attractiveness of Germany, **Elliott Management** – long focused on arbitrage opportunities in the country – is adopting a new tactic. The hedge fund is targeting operational improvements at **GEA** and squeezed a higher price from **Stada**'s sale to private equity firms Bain and Cinven.

Yet one activist that has shunned the country for the past few years is **Cevian Capital**. An investment in **Bilfinger** – made in 2011 – was a flop, with the activist itself admitting it had made a mistake, while a campaign at **ThyssenKrupp** has produced mixed results. ThyssenKrupp reportedly declined to pursue a breakup plan and instead announced a deal to merge its European steel unit with **Tata Steel**, a combination Cevian believes will not yield its desired synergies.

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Incipient stage

Despite many reasons to expect an uptick in activity in the coming years and optimism from funds, activists interviewed by *Activist Insight Monthly* acknowledge that the market is still at an incipient stage and will probably never reach U.S. or U.K. levels, even on an adjusted basis.

Till Hufnagel, a partner at **Petrus Advisers**, compares the emergence of activism in Germany today with the sudden arrival of private equity strategies almost two decades ago. “Within two to three years, Germany became one of the most developed private equity markets in Europe, if not in the world, because people understood how it works - it can drive economic growth - and [they] accepted it,” Hufnagel maintains.

He believes activism could become successful if it is adapted to Germany’s

cultural and legal framework. U.S.-style activism – often considered aggressive and contentious – may not work in Germany, Hufnagel admits, but **Active Ownership Capital (AOC)** recently won a surprise victory in a proxy contest at **Stada** in 2016.

“Another element expected to benefit activism is the European Union’s effort to improve corporate accountability.”

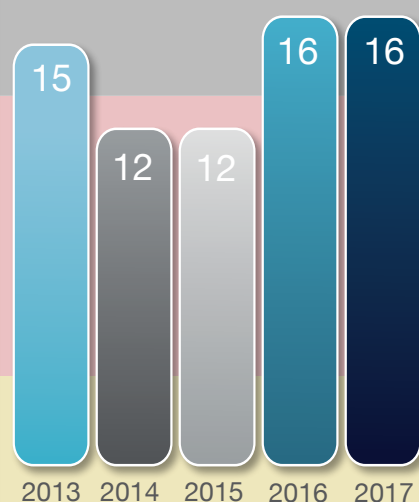
Changing premises

Chief among factors that may contribute to increased activity in the coming years is the changing

shareholder structure of German companies, according to Klaus Roehrig, AOC’s founding partner and former head of Elliott Management’s investments in the German-speaking region. “The ownership of medium and large companies - DAX companies, in particular - is now geared towards U.S. and maybe U.K.-dominated funds and the like, such as **BlackRock**, **Fidelity**, **Vanguard**, and **State Street**” Roehrig says. “They are now a much more dominant shareholder group of DAX companies compared to five or ten years ago.”

Foreign entities are more likely to embrace activism and become more active themselves than domestic institutions, Roehrig argues. Yet German investors are increasingly more favorable to activism as they hunt for higher returns. “Because of the low-yield environment, [German institutions] are more willing to consider supporting an activist. At least, if the activist has

Activist targets in Germany



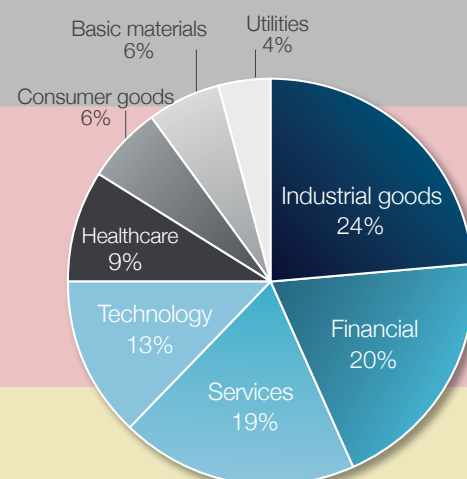
Number of Germany-headquartered companies publicly subjected to activist demands by year.

Germany success rate

66%

Percentage of public activist demands at least partially satisfied since 2013.

Germany sector breakdown



Rounding may cause summation errors.

Sector breakdown of the Germany-headquartered companies publicly subjected to activist demands since 2013.

“Because of the low-yield environment, [German institutions] are more willing to consider supporting an activist. At least, if the activist has a credible case and management has little credibility.”

a credible case and management has little credibility,” he suggests.

Out of the spotlight

A specific characteristic of German activism is that most of it still happens behind-the-scenes. Both Roehrig and Hufnagel admitted that they typically go public with their demands only when management teams decline to engage amicably. The lack of data makes it difficult to quantify the true amount of activism in the country, as opposed to the U.S., where investors are obliged to disclose details about their engagement if they cross the 5% ownership threshold.

One U.S. investor active in Germany says all his campaigns have become public. **Guy Wyser-Pratte**, the founder of the eponymous hedge fund, has run over 100 campaigns in Europe over the past 23 years, including a highly-successful one at Germany’s **KUKA** in 2009. Wyser-Pratte concedes that

the environment is tough for activists, singling out the corporate governance code of voluntary compliance, which in his view has “no teeth.”

German companies should either comply with various elements of the code or explain why they are not doing so, leading to abusive situations on the side of management teams. “You can’t get companies to behave properly,” Wyser-Pratte complains. His latest target is a case in point. **OHB**, a family-controlled aerospace company, has refused to give him a board seat, despite admitting that it cannot create committees because its three-member board is too small.

On the other hand, the France-born U.S. activist maintains the code’s shortcomings make Germany attractive from a valuation standpoint. “The discounts are very great,” he says. “In the U.S., everything trades at multiples of book value. That’s not the case in Europe.” Low valuations create much low-hanging fruit, with discounts easily closed via assets sales, restructurings, or fixing corporate governance malfunctions, according to Wyser-Pratte.

Summer of discontent

All three activists have been busy this year, particularly in the last few months.

AOC gained one seat at **Schaltbau Holding**, a company producing door systems for buses and railways, following a proxy contest and is on track to appoint an additional director. Petrus Advisers has been active at comdirect, an online bank majority-owned by **Commerzbank**.

Another element expected to benefit activism is the European Union’s (EU) effort to improve corporate accountability. The EU amended the shareholder rights directive this summer with the express aim of boosting shareholder engagement, particularly on executive pay. The amended code, which will be effective in roughly two years, requires companies to conduct votes on remuneration policies, which are expected to be binding unless member states opt out.

“[The new EU directive] means that historically passive institutions have to build up departments or get external support in deciding on AGM agenda points, in particular, whether they should support the compensation scheme or not,” Roehrig says. “I think this trend will continue. Governments are incentivizing shareholders to become more active and take responsibility.” 🇪🇺

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Activist Investing in Europe

A special Activist Insight report in association with Skadden, Arps, Meagher & Flom.

Coming this November.



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