

“Corporate Governance Through Voice and Exit”

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5 October 2019

The research was supported by a grant from the Norwegian Finance Initiative (NFI).



What do we know about shareholder stewardship?

	Passive Manager	Active Manager	Activist Hedge Fund
Stakes held	Hundreds to thousands	Hundreds	Typically <20 companies
Fund can vote/complain/engage (“Voice”)	Yes	Yes	Yes
Fund can SELL (“Exit”)	No	Yes	Yes
Workload per Governance team member	~250 companies per person, per year	~20 companies per person, per year	~1 company per person, per year

Note: Activist hedge funds are a highly specialized market. Represented less than 1 percent of global equity assets in 2015 (despite large and persistent inflows)

What do we know about shareholder stewardship?

“[W]e have little direct knowledge regarding how institutional investors engage with portfolio companies, as many of these interactions occur behind the scenes—unless institutions publicly express their approval or disapproval of a firm’s activities or management, their preferences and private engagements with portfolio firms are not observable.” (McCahery, Sautner and Starks 2016)

Our study

- Proprietary data from a large UK asset manager: Standard Life Investments (SLI; today Aberdeen Standard Investments)
- Data on contacts with portfolio companies (engagements), voting and daily holdings (trading) for all funds with a UK equity position
- Study focuses on UK equities team
- Caveats
 - » Proprietary data, difficult to replicate
 - » Single asset manager with specific stewardship & investment process
 - » Voluntary disclosure bias

Research questions

We attempt to provide evidence on:

1. How is the SLI UK Equities Team organized?
2. How does SLI monitor, how does it engage, and how does it vote?
3. What role does monitoring, engagement and voting play in trading decisions ?
4. Does monitoring and engagement provide information advantages?
Does it contribute to alpha?

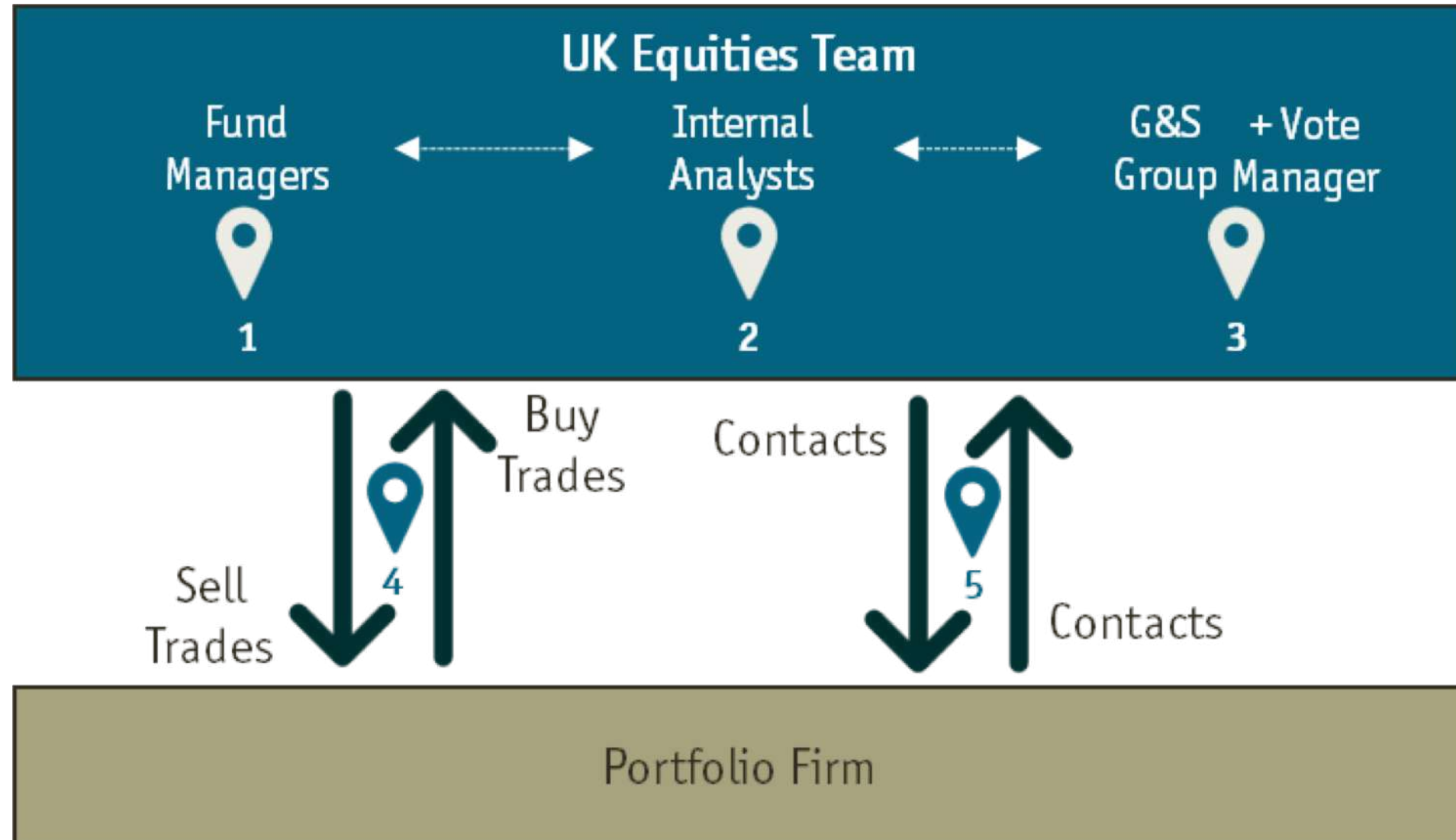
Institutional Setting

- SLI Funds Managed by the UK Equities Team
- UK Equities Team
 - » Governance and Stewardship Group
 - » Internal Sector Analysts
 - » Fund Managers
 - » Vote Manager
- Activities
 - » Monitoring and engagement (meetings, other contacts)
 - » Voting
 - » Trading

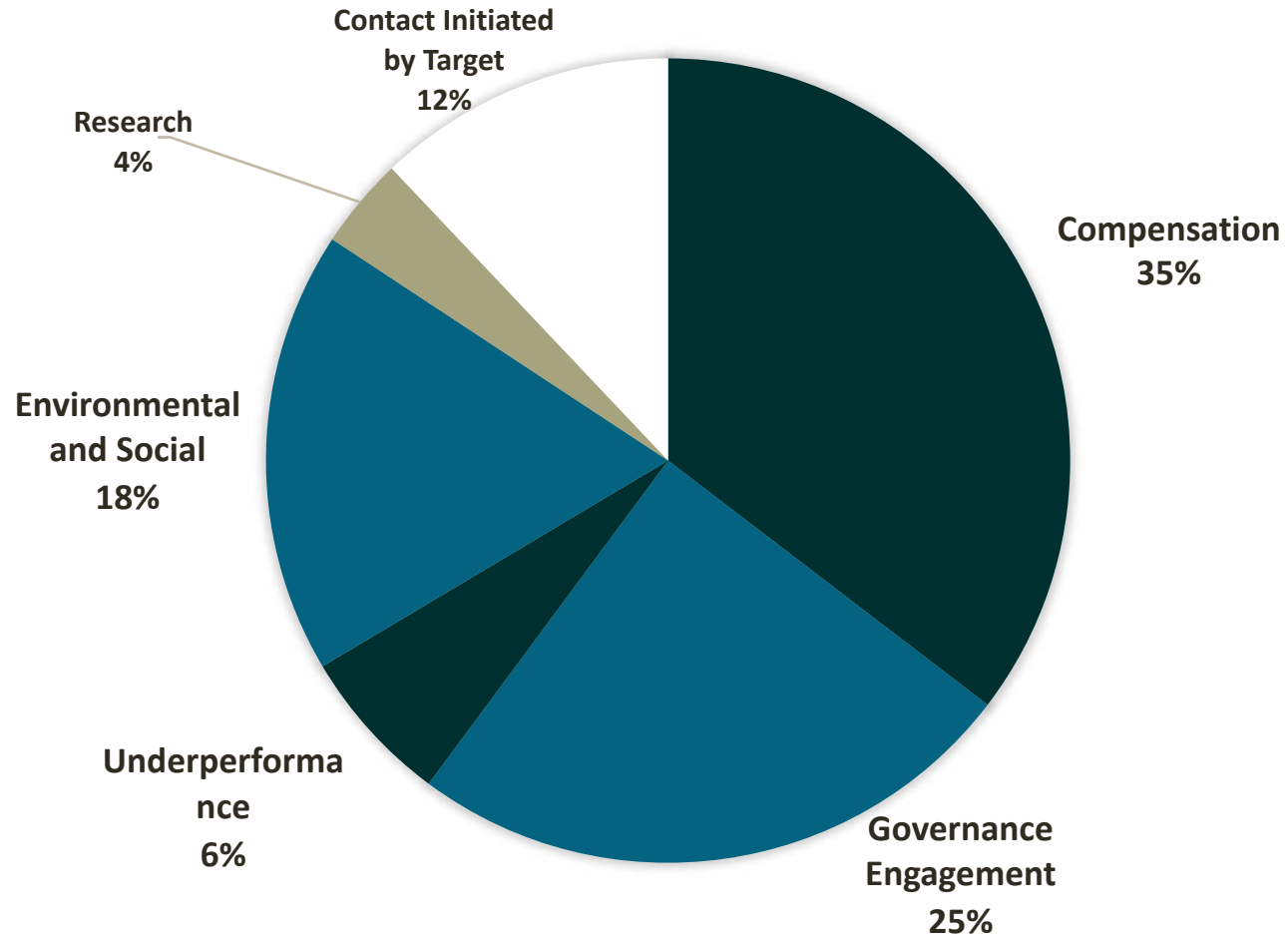
SLI is usually one of the largest investors of its portfolio firms. To illustrate, meetings with the portfolio firms are usually attended by CEO, or Chairman, or both

Panel A: Holdings

Date	FTSE All Share Stocks	Stocks Held by asset manager	Average Aggregate Stake Held	Number of Funds	Number of Positions across all Funds	Aggregate TA (\$ billions)
2007m6	692	369	2.98	60	5356	66.5
2007m12	706	379	3.02	64	5880	63.0
2008m6	670	378	3.19	63	6266	53.1
2008m12	671	376	3.10	61	6287	28.7
2009m6	624	364	2.94	60	6485	30.4
2009m12	626	366	2.88	57	6183	38.8
2010m6	645	367	2.87	57	6098	31.1
2010m12	630	367	2.67	52	5730	40.8
2011m6	643	359	2.65	49	5475	42.6
2011m12	628	352	2.65	48	5121	35.5
2012m6	628	343	2.61	46	4939	33.0
2012m12	606	325	2.61	46	4746	37.5
2013m6	618	316	2.69	46	4416	39.1
2013m12	622	323	2.66	44	4156	46.9
2014m6	649	327	2.77	43	3966	47.2
2014m12	647	329	3.23	51	4343	51.0
2015m6	659	333	3.17	50	4092	50.8
2015m12	646	323	3.22	48	3713	45.8



G&S Team's motives for contacts and engagements



Note: Compensation is a frequent topic; financial underperformance is rarely a topic

Panel C: G&S Engagement – Contacts, Issues, Workload, Governance Health Warnings

Year	Contacts (<i>N</i>)	Issues (<i>N</i>)	Team members involved (<i>Avg</i>)	Workload - target firms handled per team member (<i>Avg</i>)	Percent of all stocks engaged (<i>Avg</i>)	Percent of all stocks with GHW
2007	542	504	10.0	31.8	0.39	0.07
2008	567	526	8.0	36.5	0.43	0.09
2009	534	460	11.0	24.5	0.46	0.09
2010	454	418	10.0	25.6	0.46	0.10
2011	556	494	11.0	25.5	0.46	0.11
2012	552	486	13.0	20.5	0.44	0.11
2013	492	427	12.0	21.4	0.44	0.10
2014	612	507	16.0	17.4	0.40	0.08
2015	564	430	15.0	17.4	0.32	0.05

Intensity of buy, hold and sell signals by internal analysts

Panel A: Analyst recommendations

Year	Buy			Hold			Sell		
	SLI	I/B/E/S		SLI	I/B/E/S		SLI	I/B/E/S	
2007	50.7	48.9	ND	36.5	38.5	ND	12.8	12.6	ND
2008	43.1	49.2	***	39.8	37.4	ND	17.1	13.4	***
2009	45.3	47.6	ND	36.4	36.1	ND	18.3	16.3	*
2010	49.5	53.8	***	37.2	35.1	***	13.3	11.1	***
2011	43.7	52.8	***	41.2	35.6	***	15.1	11.6	***
2012	41.3	51.1	***	38.6	36.8	*	20.1	12.1	***
2013	37.7	48.4	***	40.1	39.8	ND	22.2	11.8	***
2014	34.7	50.2	***	38.5	40.5	ND	26.9	9.2	***
2015	33.3	47.4	***	42.1	42.0	ND	24.6	10.6	***

Panel B: Analyst recommendation changes, frequencies

Signal	Buy to Hold	Buy to Sell	Hold to Sell	Sell to Hold	Sell to Buy	Hold to Buy
Number of unique changes	772	86	519	480	81	722
Number of affected positions	16133	1561	7027	6072	884	12385
Days	235.1	210.8	129.4	126.8	138.7	127.0

Panel D: Voting

Year	Number of meetings voted at	% of meetings where asset manager casts a vote on at least one management proposal		
		Vote against	Abstained	Any Disagreement
2007	766	6.8	10.1	13.4
2008	764	5.9	9.8	12.7
2009	487	14.0	17.9	27.9
2010	452	8.4	11.7	18.6
2011	442	11.1	14.0	21.7
2012	418	20.8	12.0	28.7
2013	392	13.5	11.0	23.0
2014	433	10.9	15.7	24.7
2015	445	9.9	14.2	22.0

Panel E: Voting and portfolio exposure

	No Disagreement	Vote against	Abstain	Any Disagree (Vote against or Abstain)
Number of shareholder meetings	4081	411	499	791
Number of outstanding positions	42,161	11,582	11,123	18,317

Event Study

Event study of trading and abnormal returns around four events:

- I. Company meetings
- II. Raising of internal governance warning
- III. Internal analyst recommendations
- IV. Voting

Event Study

- I. **Company meetings – TO COME!**
- II. Raising of internal governance warning
- III. Internal analyst recommendations
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Event Study

- I. Company meetings
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Trading Around Governance Health Warning Events

Panel A: Trades around Governance Health Warnings, alternative windows

	-25 to +25		-50 to +50	
	<i>N</i>	Percent	<i>N</i>	Percent
No trade	11	0.25	7	0.16
Trade - net buyers	970	21.69	823	18.56
Trade - net sellers	3,492	78.07	3,643	81.44
Total positions	4,473	100.00	4,473	100.00

Panel B: Trading decisions – net sellers

	-25 to +25	-25 to -6	-5 to -2	-1 to +1	+2 to +5	+6 to +25
Abnormal trades based on Shares Held	-16.56*** [0.834]	-3.701*** [0.458]	-0.560*** [0.185]	-0.709*** [0.224]	-2.201*** [0.378]	-10.15*** [0.473]
<i>N</i>	4,473	4,455	4,470	4,473	4,473	4,448
Abnormal Trades based on <u>Mcap</u> Held	-17.22*** [0.851]	-4.287*** [0.469]	-0.382* [0.204]	-1.864*** [0.201]	-3.292*** [0.374]	-9.184*** [0.503]
<i>N</i>	4,473	4,455	4,470	4,473	4,473	4,448

Event Study

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Analyst Recommendation Information Content and Fund Manager Trades

Panel A: Trades for Sell and Buy changes, -1 to +5 window

	Any Sell Signal		Any Buy Signal	
	<i>N</i>	Percent	<i>N</i>	Percent
No stake	6	0.0	6	0.0
No trade	18510	74.9	15,975	82.4
Trade - net buyers	748	3.0	2,624	13.5
Trade - net sellers	5460	22.1	785	4.1
Total positions	24724	100.0	19390	100.0

Panel B: Trades of net sellers and net buyers

	-1 to +1	-1	0	1	+2 to +5
	Any Sell Signal				
Shares Held – net sellers	-17.10*** [0.255]	-0.971*** [0.0401]	-8.026*** [0.171]	-6.469*** [0.134]	-14.46*** [0.270]
<u>MCap</u> Held – net sellers	-20.0*** [0.28]	-2.19*** [0.092]	-9.80*** [0.19]	-7.30*** [0.15]	-15.0*** [0.31]
	Any Buy Signal				
Shares Held – net buyers	24.69*** [0.608]	0.0393* [0.0216]	4.667*** [0.279]	6.117*** [0.202]	15.57*** [0.474]
<u>MCap</u> Held – net buyers	29.8*** [0.80]	0.21 [0.21]	8.35*** [0.39]	7.93*** [0.27]	17.1*** [0.62]

Analyst Recommendation Changes and Performance

Days	-1 to +1	-1	0	1	+2 to +5
Any Sell Signal - at least one fund net seller	-2.91*** [0.25] 680	-0.47*** [0.11] 680	-1.77*** [0.18] 680	-0.54*** [0.097] 680	-0.54*** [0.17] 680
Any Sell Signal - at least 25% of funds net sellers	-3.46*** [0.39] 309	-0.69*** [0.17] 309	-1.85*** [0.26] 309	-0.74*** [0.14] 309	-1.03*** [0.24] 309
Any Sell signal - no fund net seller	-1.86*** [0.24] 526	-0.41*** [0.10] 526	-1.19*** [0.17] 526	-0.25** [0.099] 526	-0.40** [0.16] 526
Any Buy Signal - at least one fund net buyer	1.61*** [0.29] 463	0.036 [0.15] 464	1.27*** [0.19] 463	0.37*** [0.12] 464	0.70*** [0.22] 464
Any Buy Signal - at least 25% of funds net buyer	2.01*** [0.47] 201	0.00086 [0.22] 202	1.64*** [0.31] 201	0.32 [0.21] 202	1.27*** [0.35] 202
Any Buy signal - no fund net buyer	1.48*** [0.16] 1,220	0.12 [0.082] 1,223	1.08*** [0.11] 1,220	0.30*** [0.071] 1,223	0.30** [0.13] 1,223

Analyst Recommendation Changes and Performance

Panel B: Abnormal returns to trading, 0 to +5

Sell Trades					Buy Trades				
(1) As if passive	(2) Active Trading optimistic	(3) Active Trading pessimistic	(4) <u>Dif</u> optimistic	(5) <u>Dif</u> pessimistic	(6) As if passive	(7) Active Trading optimistic	(8) Active Trading pessimistic	(9) <u>Dif</u> optimistic	(10) <u>Dif</u> pessimistic
-3.506***	-3.029***	-3.287***	0.477***	0.219***	2.291***	2.968***	2.515***	0.678***	0.224***
[0.0865]	[0.0750]	[0.0776]	[0.0262]	[0.0225]	[0.140]	[0.199]	[0.177]	[0.0897]	[0.0628]
4,467	4,467	4,467	4,467	4,467	2,365	2,365	2,365	2,365	2,365

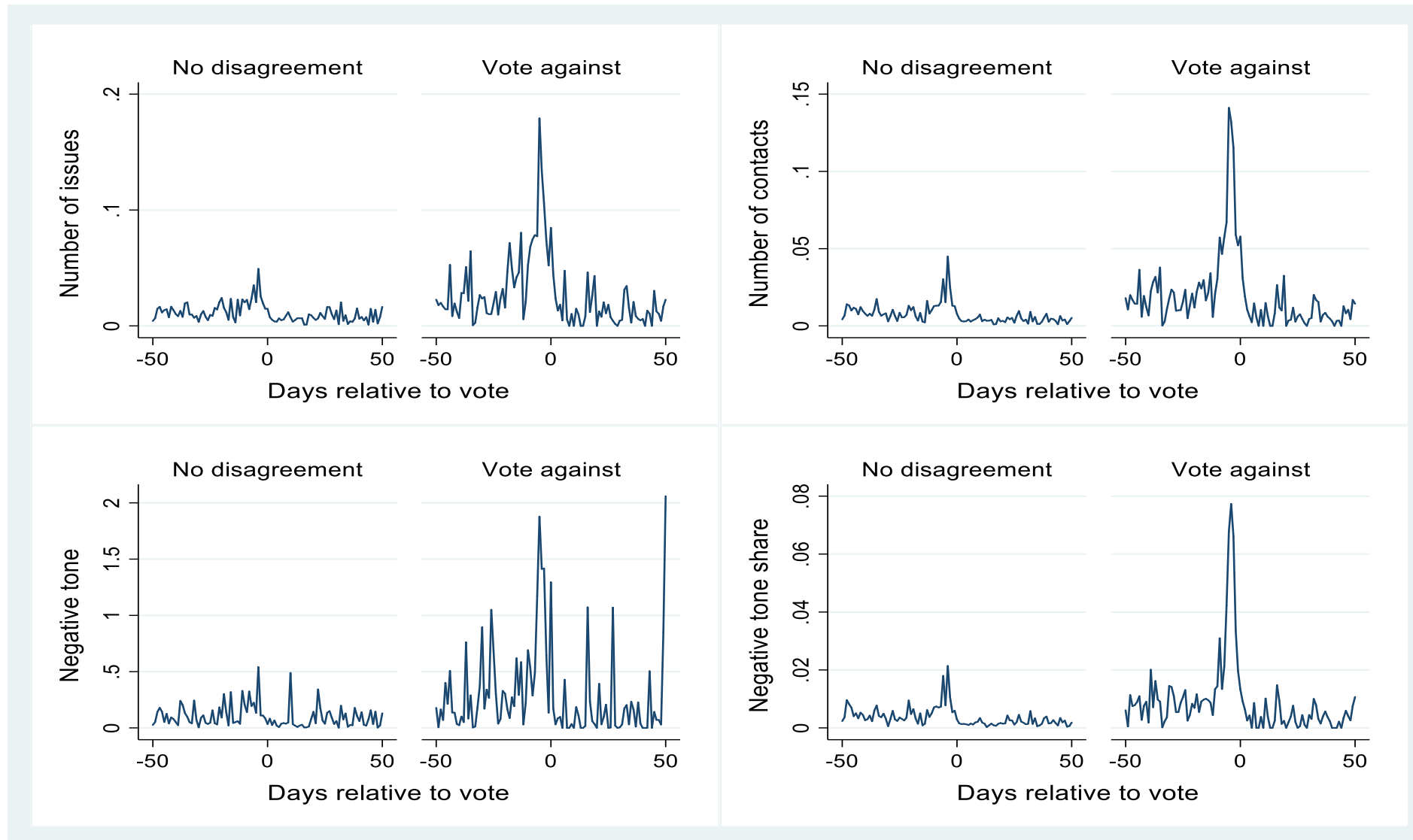
Buy-Side and Sell-Side Analyst Recommendation Changes

	Buy to Hold	Buy to Sell	Hold to Sell	Sell to Hold	Sell to Buy	Hold to Buy
SLI	-2.80***	-5.22***	-4.96***	-1.59***	3.64***	1.52***
	[0.095]	[0.39]	[0.20]	[0.44]	[0.23]	[0.15]
<i>N</i>	3,618	443	1,398	564	143	1,909
I/B/E/S	-0.98***	-1.19***	-1.24***	0.68***	0.80***	1.07***
	[0.053]	[0.17]	[0.089]	[0.087]	[0.15]	[0.052]
<i>N</i>	9,956	1,146	3,648	3,683	1,098	9,201

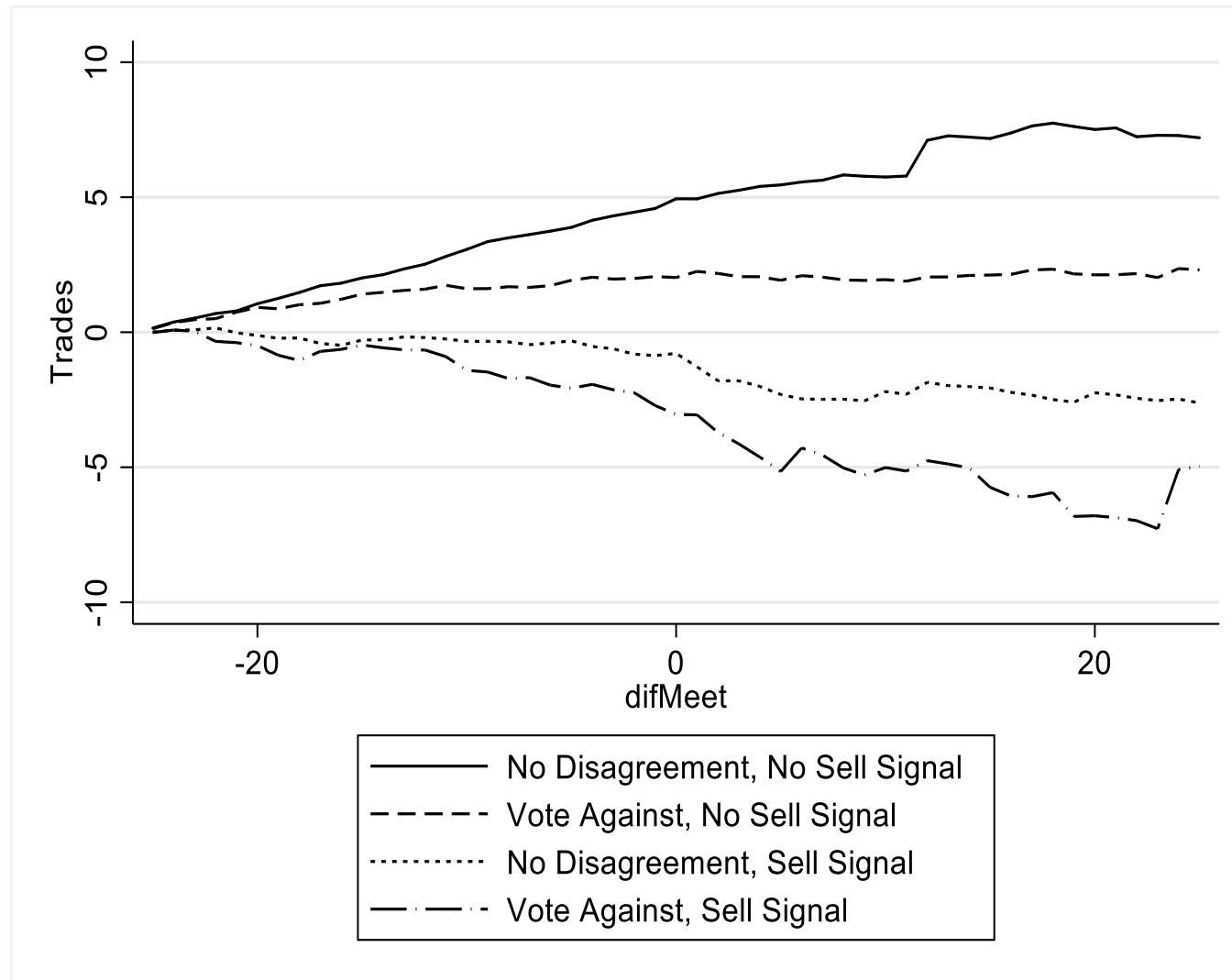
Event Study

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Engagement Activity & “Tone” around shareholder votes



Trading, analyst signals and disagreement



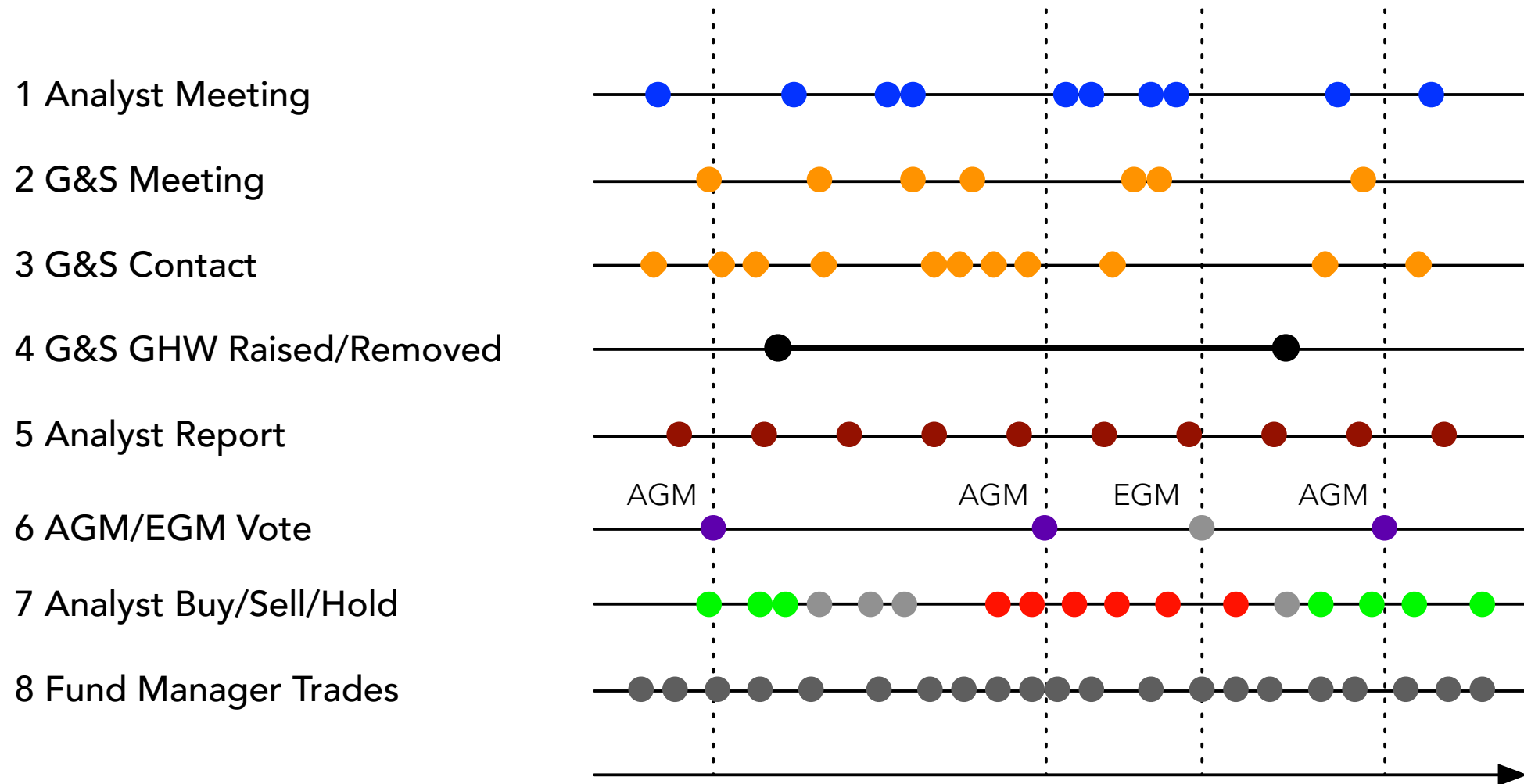
Conclusions

- How do active managers engage with portfolio firms? And, what role does monitoring and engagement play in their trading decisions? We use proprietary data to answer these questions.
 - » Internal analysts and a centralised stewardship team monitor the board and management and place portfolio companies on a watch list when there are governance or other concerns.
 - » The asset manager engages more intensively with the watch list, abstaining or voting against management proposals in a third of meetings.
 - » More intensive engagement and negative votes against are associated with internal analyst downgrades and with exit by fund managers.
- We provide evidence that monitoring and engagement generate information advantages, which in turn contribute to alpha. Our results provide strong support for voice influencing exit.

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Panel B: Sector Analyst Meetings

Year	Number of Meetings	Companies Met per Year	Coverage (%)	CEO Present	FD Present	Chair Present	CEO and FD Present	CEO, FD or Chair Present	(in %)
2007	668	338	89.2	393	348	39	273	486	72.8
2008	622	334	88.8	332	303	24	227	417	67.0
2009	693	337	92.1	364	330	31	258	451	65.1
2010	666	319	86.9	368	361	29	275	469	70.4
2011	688	327	92.9	387	335	32	261	479	69.6
2012	674	338	100.0	368	321	31	236	466	69.1
2013	685	336	100.0	355	281	14	215	426	62.2
2014	663	331	100.0	360	263	10	195	431	65.0
2015	650	330	100.0	331	237	15	182	394	60.6



Acknowledgement

We are very grateful to

Norges Bank Investment Management and its Norwegian Finance Initiative (NFI) for financial support and

Standard Life Aberdeen (SLA) for data access, discussions and patience.