



IR HOT TOPIC: The Modern Era of Shareholder Activism

The New Class of Shareholder Activism. Shareholder activism in the 21st century has reclaimed the high profile it had in the late 1980s, with a few differences. Today, hedge fund and private equity managers, such as Carl Icahn, are leading this modern-day movement versus the buyout kings of Michael Milken and T. Boone Pickens Jr. What also has changed is that hedge funds now manage an estimated \$1 trillion, up from \$400 million five years ago. As a result, they are teaming up together to take on companies, small and large, boosting their odds of bringing change compared with their counterparts of the past.

Here's a closer look at billionaire financier Carl Icahn and his views on 'imperial CEOs' in the February 26th issue of *Time* magazine. The interview is titled, "10 Questions for Carl Icahn." The following are a few interesting excerpts: "You make quite a lot of money. Isn't complaining hypocritical?" Carl responded, "I'm not against a CEO making a lot of money if the stock goes up and he has options. What's unconscionable is when the stock goes down and they reprice the options. CEOs are paid for doing a terrible job." Another question posed, "Do you accomplish anything besides making money?" Carl said, "Yes. America is going to lose its economic hegemony if we don't do something along the lines of what I'm doing, where you make managements accountable. Our companies are really not competitive with Asia, and this is the great new threat."

WHO ARE THESE ACTIVISTS

Activist hedge funds have grown significantly in the past three to five years with an estimated 90 corporate activist hedge funds worldwide today. Those

who frequently make headlines include such names as: *Steel Partners, Relational Investors, Third Point, Cannell Capital, Jana Partners, Tracinda, Pirate Capital, Bulldog Investors, Appaloosa and Pershing Capital*. The strategies engaged in by activist hedge funds vary and are multiplying. Three popular strategies include corporate governance, ownership and buy out efforts or financing. Activists typically identify a company that is undervalued. It then figures out how the share value of the company can be increased. After this, it slowly starts acquiring shares of the company from the market. Once it has a substantial stake in the firm it starts demanding changes in the company policies or strategies from the management, including the company's M&A decisions, the capital structure, forcing a sale or break-up of the company, cutting costs, firing management, or modifying a board's composition.

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-Carl Icahn

ACTIVIST TARGETS

A compelling force for shareholder activism is first and foremost a persistently underperforming stock. But that's usually just one piece of the puzzle. Following are a few other prevalent factors that drive activism:

- Surplus of cash on the balance sheet with no plans for its use via a share buyback, dividend or acquisition.
- Operational and financial underperformance compared to peers.
- M&A opportunities rejected by company.
- Inconsistent and unclear communication strategy.

The Modern Era of Shareholder Activism....continued

MANAGING ACTIVISTS

Clearly, the activist movement is a corporate reality that must be managed and addressed when appropriate. Following are a few suggestions on how to deal with shareholder activism:

- Companies should proactively and continuously review and evaluate the strategic, financial and operational options initiatives that they employ to improve the business.
- Communicate the company’s strategy clearly, succinctly, consistently and often. Management must closely keep an eye on and communicate their plans on capital structure and allocation.
- Executives who develop and foster relationships with activists, compromising with instead of avoiding them, actually do a better job of keeping them at bay – and keeping their own jobs.
- Maintain relationships and keep lines of communication open with top shareholders as dissident shareholders will likely seek out other large shareholders for their support.
- Proxy advisors such as ISS, Glass Lewis and Proxy Governance can be powerful as they advise shareholders on how to vote their proxies. Thus, it is important for companies to work with these independent third-parties.

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 - Anonymous IRO

To reiterate our points and illustrate first-hand experiences with shareholder activism, we interviewed an Investor Relations Officer who asked to be anonymous. The IRO said, “Be nice to hedge funds but don’t court them. If management does not deliver, the stock will weaken so then beware...hedge funds smell blood and travel in packs. Or, it’s best to weigh your chances of winning a proxy fight before taking it to the mats. It’s like a court case, sometimes you win by settling.” Also offering expertise on shareholder activism, Jason Rubin, President and Founder of The Redstone Group, a communications consulting firm based in West Conshohocken, Pennsylvania, commented, “If a shareholder files a 13G or press release to express their disappointment with management or suggest other intentions, I would not comment on their filings but begin pre-

paring for the possibility of a more public dispute about management’s record. Investors have rights to express how they feel, and management should engage and have open relationships with their shareholders.”

WHAT’S AHEAD

Proxy fights hit highs in 2006, and more is forecasted for 2007. Investors looking to advocate change at publicly traded companies are ever more fighting and successfully winning seats on boards, a trend that’s expected to continue in 2007. According to SharkRepellent.net, a website dedicated to corporate takeover defenses, last year, the number of disputed board elections surged to 91, the highest it’s been since the onset of the tracking of this data in 2001. In comparison, there were just 40 battles for board seats in 2005 and 30 the year before. The number of proxy fights could notch even higher in 2007. Sharkrepellent.net has already tracked 32 proxy contests for 2007, 28 of which include efforts to obtain board representation. According to proxy watchers, industries that could be targets in 2007 comprise of restaurants and technology companies as evidenced by the companies already facing proxy battles. As tracked by Sharkrepellent, the majority of companies engaged in board contests tend to be small, with 87% of targets so far this year consisting of companies with market capitalizations under \$2 billion. Larger companies are not off the hook, although conducting proxy fights with them can require substantially more money.

IN SUMMARY

Companies respond to and manager shareholder activism differently. Some engage in active public dispute about the issues while others remain silent. The better strategy should be to directly deal with the issues raised by activists as even non-activist shareholders expect companies to respond. Ultimately, communication is the foundation for good governance and uncontested proxies.

For questions or comments, contact Kasha Widner, Senior Associate at Ilios, (312) 261-6455 or kwidner@ilios.com.



irNavigator & Shareholder Activism. irNavigator, Ilios' online investor relations platform, has been at the forefront of tracking activist hedge funds and investors. irNavigator diligently categorizes activist investors based on their past corporate actions and flags those investors so they can be easily identified when they appear in your shareholder list. In addition, irNavigator users can track archived stories about activists which are linked by contact, firm, and issuer. Not only do the archives and flags help you to never be surprised by a new activist shareholder, it also allows you to review the type of action you can expect from each activist. Being prepared when an activist firm confronts senior management is the first step in communicating effectively with the aggressor. To review irNavigator's activism archive or if you have any questions about the product, please call (646) 519-3333.

About irNavigator. *A Fast, Intuitive Platform for the Investor Relations Professional.* In your office or on the road, the importance of accurate, timely information has never been more essential. irNavigator brings together the latest technology, Ilios' proprietary ownership, contact and profile databases and an integrated Contact Relationship Management (CRM) offering into one solution. irNavigator has been built using focus groups and client feedback; everything from the data to the underlying functionality of the product has been built with one thing in mind – to provide a product that is fast and easy to use with comprehensive and accurate data.



our entire organization as an extension of their IR department. Whether the need is for a board report or an internal deadline that needs to be met, we will use our accumulated expertise, resources and 'best of breed' networking with our clients to provide the best products and services for our customers.

A Letter From Our CEO...

Looking back at my origins in Investor Relations in the mid-80s, when hostile takeovers and greenmail was the order of the day, it is evident to me how far the IR function and the tools available have progressed. While the landscape has certainly changed dramatically, there are some things that ring true today more than ever....**Customer Service.**

We're passionate about what we do.

At Ilios, we're extremely proud of the professionals that make up our organization and are also proud of the fact that we are the most experienced Capital Markets Intelligence firm in the industry. Furthermore, Ilios is now the second largest CMI firm and the largest privately held firm- all through organic growth. Summing it all up, we're passionate about what we do and it shows.

How many hats do you wear?

Today, the Investor Relations function has never been more important to upper management, while the investor community has never been more sophisticated and demanding. These facts combined with the ever expanding role (and sometimes decreasing budget) of the IRO compels Ilios to continue to remain in the forefront of creating effective, value-added and innovative methods to service the ever evolving environment of our clients.

No job is too difficult or great.

In response to the changing needs of our clients, we encourage all of our partners to treat their Ilios contact and

We're a boutique firm and we're experts at what we do.

Ilios is able to respond to the marketplace in a much more efficient and effective manner, because we are a boutique firm where all of the 'partners' are actively managing our business. Additionally, we are positioned in the market to be flexible to accommodate almost any request and situation. We are also unique in that all of our employees are accountable first to the client and then to the senior partners including myself, who all continue to provide preeminent services personally.

On that note, I highly encourage our clients to call me directly at (312) 261-6414 for any issue, comments or questions. I would also be more than happy to visit your offices or invite you to visit ours, so that we may continue to build a stronger partnership.

Sincerely,

Nick Trikolos