Market Intellect
from Global Markets Intelligence

Sector Disruptors: Investor Activism

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We have reached a golden age of investor activism. In the past five full years, activist engagements increased fourfold. Furthermore 64 activist cases have been announced thus far in 2015 (through June 19, 2015) compared with only 18 total transactions in all of 2005 and 102 for 2014, according to S&P Capital IQ data. The success of investor activism has helped these firms both attract more capital and deliver greater returns as their principals now regularly make news and headline events. Many of them have become household names who literally move markets. Better understanding investor activism means better understanding global markets.

We believe a number of factors have contributed to the increasing actions and impact of activist investors, including:

- A strong stock market in a low interest rate environment;
- Greater pressure on managements to deliver performance;
- Limited top-line growth for most companies;
- Large and growing corporate cash balances;
- More acceptance of so-called "financial engineering"; and
- Notable activism with positive results.

Although fundamental and stock underperformance relative to industry peers is clearly the primary driver for activism across the overall equity space, S&P Capital IQ Global Markets Intelligence (GMI) Research has also noticed specific sector-based themes that have led to greater activist interest. We have highlighted some of the high-profile activist cases in the tables below. These themes could lead to further activity ahead.

Consumer discretionary, which has had the greatest number of instances in the past decade, has attracted many activists given its fragmentation across a relatively broad array of subindustry groups. As a result, we think this makes the sector ripe for more industry consolidation and spin-offs.

Within the information technology sector, corporations amassing and hoarding large cash balances have attracted new activist positions. We also note the sector's more favorable valuations today relative to historical levels make it a prime candidate. In the industrials area, participants with illogical vertical integration or multiple unrelated businesses have become activist targets.

The telecommunications services and utilities sectors have had the lowest levels of activism, largely reflecting the highly regulatory environment associated with the companies. In addition, businesses within these sectors tend to possess highly leveraged balance sheets and low cash levels that also make the space unattractive for activists.

Activism takes shape when an investor buys shares and/or equivalents to put pressure on corporate direction or shareholder goals. The agendas vary among investors and focus on specific areas, including cost reductions, reorganizations, corporate spin-offs, revamped financing structures, greater leverage, and more shareholder-oriented uses of cash and liquidity to realize higher enterprise value in the public markets.

Investor activism has become a leading influence in our capital markets today unlike in the past when these so-called corporate raiders were viewed as an anomaly for public company dealings. Now they are shaping boardroom discussions regardless if a company has been "targeted directly or indirectly with activity in its peer group."

Corporate governance (e.g., issues related to executive compensation, board representation, proxy contests, strategic matters) has also been affected by how management and board of directors decide where to apply available resources. This has progressively led to a shift from reinvesting in the business to allocating a greater percentage of capital toward share repurchases and dividends.

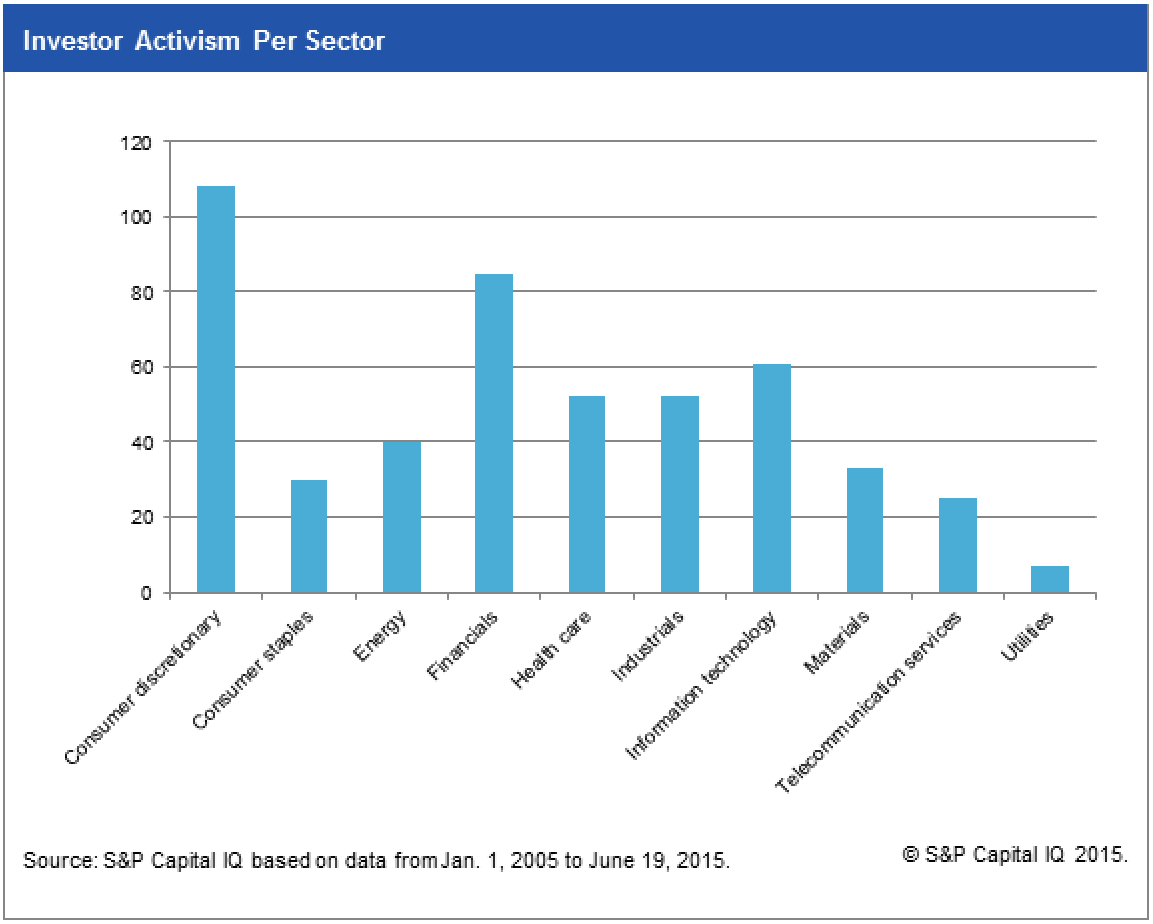
Many have asked about the power and performance of activists, but one thing is not in doubt: the increased volume of their actions in the past decade.

Applying S&P Capital IQ's data and analytics, we identified just fewer than 500 examples of investor activism involving companies with individual market capitalizations of $1 billion or more from the beginning of 2005 to mid-2015:

- From 2005 to 2009, 89 activist actions occurred. In the past five years, from 2010 to 2014, 341 actions took place.
- We have seen volume increases for every year since 2010, and this trend has continued strongly in 2015.

In our Sector Disruptors series, our equity analysts focus on both top-down and bottom-up considerations for sectors, industries, and stocks, leveraging data and analytics from S&P Capital IQ. As in the past, our equity analysts conduct research and analysis from a sector perspective for all 10 of the Global Industry Classification Standard (GICS) economic sectors to provide differentiated insights and to identify potential opportunities.

Chart 1



Consumer Discretionary

From retailers, restaurants, and film studios to automotive companies and providers of specialized consumer services, the consumer discretionary sector has had relatively rife investor activism. Indeed, the sector has far outpaced others on the volume of activist disclosures in the past 10 years. We infer that a majority of such activist campaigns were launched since 2014--coincidentally with the first year of the sector's relative stock underperformance versus broader market indices after sizable outperformance since 2008.

Across the sector, activist investors have advocated for mergers or spin-offs, management or governance changes, and new or accelerated share buyback programs, among other corporate actions. In doing so, they have engaged in tactics including board representation requests, takeover bids, and, increasingly, proxy contests. Not surprisingly, such campaigns have produced a range of outcomes.

Sector activism examples

In a rare resounding victory after a protracted campaign, activist investor Starboard Value L.P. successfully ousted the entire 12-person board of Darden Restaurants Inc. (Darden) in 2014, after the company rebuffed its proposal to spin off its Olive Garden and Red Lobster chains and instead sold the latter. In June 2015, Darden followed up with an announcement of plans to spin off certain restaurants into a REIT in a move that aims to exploit the "valuation differential between restaurant and real estate companies."

In a different compromise scenario, activist Dan Loeb's Third Point LLC secured three seats on Sotheby's 15-member board in 2014. The move followed a blistering campaign in which Loeb referred to the auction house as "an old master painting in desperate need of restoration." After a recent ouster of its CEO, Sotheby's faces a fresh activist campaign by Marcato Capital Management LLC, which demanded an immediate $500 million in share repurchases and the replacement of the company's chief financial officer.

In addition to boardroom changes, activists have successfully instigated a sale (or potential sale) of some notable consumer discretionary companies to competitors. In late June 2015, Pep Boys: Manny, Moe & Jack, under a new CEO named that month, unveiled plans to explore strategic alternatives because several parties indicated potential interest. This came after some prodding by activist investors, including Mario Gabelli's Gabelli Asset Management Company Investors (GAMCO), which owns a 19% stake. Furthermore, in 2014, Carl Icahn coaxed Family Dollar Stores Inc. to be acquired by Dollar Tree Inc. in an $8.5 billion transaction that could close in July 2015 (Nelson Peltz's Trian Fund Management. L.P. had unsuccessfully bid for Family Dollar in 2011). More recently, in February 2015, Starboard Value L.P. also nudged Office Depot Inc. toward a $6.3 billion acquisition by Staples Inc. that could close this year.

Activists played key roles in Men's Wearhouse Inc.'s $1.8 billion acquisition of Jos. A Bank Clothiers Inc. in June 2014 and Ascena Retail Group Inc.'s pending $2.2 billion acquisition of Ann Inc. Separately, to placate certain activists' requests for board representation, General Motors Co. recently acquiesced to $5 billion in share buybacks, following a 20% dividend increase.

However, the sector hasn't always been a bed of roses for activists, who on occasion have suffered some outright defeats. For example, in 2011, Icahn sold his entire 33% stake in Lions Gate Entertainment Corp. at $7 a share after retreating from a bruising three-year battle with the company that included some abortive takeover bids. Although the SEC recently levied a relatively modest fine on Lions Gate Entertainment Corp., the company's stock has risen more than five-fold since Icahn's surrender.

In another instance, Bill Ackman's Pershing Square Capital Management L.P.--following a three-year campaign during which it secured some board seats at J.C. Penney Co. Inc. after becoming its largest shareholder--unsuccessfully exited its entire position in 2013 because of futile turnaround efforts, including several management shuffles.

Potential activist opportunities

Some consumer discretionary companies could be ripe for some dose of investor activism as a potential catalyst for shareholder value. First, we think The Gap Inc. could benefit from a fresh strategic perspective with an activist investment. It has protracted fledgling turnaround efforts, culminating in several years of underperformance for its stock price even as the company sustains its share buybacks and dividend policy. Under a new management team led by CEO Art Peck since early 2015, we still see some lingering merchandising challenges for the Gap and Banana Republic divisions amid intense competition.

DreamWorks Animation SKG Inc. could also experience activist activity. In the years since its 2004 IPO, the stock has been vulnerable to a high degree of earnings volatility in tandem with a highly concentrated (and relatively narrow) slate of feature film releases. Over the past year, the company has been the subject of merger speculations that have not materialized. Amid ongoing restructuring efforts and diversification into TV and consumer products businesses, an activist investment could help actualize its potential attractiveness as a takeover target, in our view.

Table 1

Consumer Discretionary Investor Activism

Target/issuer	Announced date	Investor activist
General Motors Co.	2/10/2015	Appaloosa Management L.P.
Staples Inc.	12/11/2014	Starboard Value L.P.
Family Dollar Stores Inc.	6/6/2014	Icahn Capital L.P.
Darden Restaurants Inc.	2/11/2014	Starboard Value L.P.
Ann Inc.	11/8/2013	Engine Capital Management LLC
Men's Wearhouse Inc.	11/7/2013	Eminence Capital LLC
Sotheby's	10/2/2013	Third Point LLC
J.C. Penney Co. Inc.	10/8/2010	Pershing Square Capital Management L.P.
Lions Gate Entertainment Corp.	10/20/2008	Icahn Capital L.P.

Source: S&P Capital IQ.

--Tuna N. Amobi, CFA, CPA and Efraim Levy, CFA, S&P Capital IQ Equity Analysts

Consumer Staples

The consumer staples sector has had 29 campaigns targeting 16 companies since the beginning of 2005, according to S&P Capital IQ data. Of these actions, 14 were unsuccessful.

Although only two actions have taken place thus far in 2015, activity has increased significantly in recent years with 61% of activist campaigns occurring since 2010. Wal-Mart Stores Inc. has been the largest target of campaigns (eight), though they have all been unsuccessful, likely reflecting the Walton family's 50% controlling interest.

Corporate governance issues have accounted for the vast majority (19 of 28) of activist campaign objectives since 2005. The largest number of corporate governance issues involved board of director matters (nine occasions), including campaigns that sought to either replace or nominate new directors or change the board's composition, or that questioned its independence. Other corporate governance campaigns included issues with executive compensation (five), accountability or discloser concerns (four), and voting matters (one). In addition, activists have engaged management in an effort to maximize shareholder value on three occasions, and there was one financial matter regarding reporting and auditing issues. On five occasions, activists have approached management about strategic (three) or merger and acquisition (M&A) matters.

Sector activism

Herbalife International Inc. (a nutritional supplement maker with a $5 billion market capitalization; Herbalife) likely had the highest profile activist case in the sector in the past 10 years. Pershing Square Capital Management L.P. went public with a $1 billion short position in the company (with a March 2015 break-even in the mid-$30s per share) in December 2012. Weak share prices in 2013 attracted Icahn (18.5% ownership stake in HLF as of February 2015), George Soros (3.7%), and former Post Holdings Inc. CEO William Stiritz (8.1%).

Icahn won five Herbalife board seats and has been instrumental, in our view, in convincing Herbalife management to suspend its dividend payments in April 2014 and lever up its balance sheet in order to repurchase $1.3 billion in shares in 2014. However, Ackman appears to be committed to his Herbalife short for now.

Although activist interest in Herbalife might garner the most media attention, we believe the more important and influential transactions for the consumer staples sector involve the partnership between Warren Buffet's Berkshire

Hathaway Inc. and Brazilian private equity firm 3G Capital

The two teamed up to purchase H.J. Heinz Co. (Heinz) in 2010, which significantly expanded margins by relentlessly slashing costs with zero-based budgeting. Following Heinz' success, the partnership then agreed to purchase Kraft Foods Group Inc. (Kraft) in March 2015 as it plans to merge it with Heinz (pending Kraft acquisition approvals) to create one of the largest food companies in the world.

A key target of the merger is achieving $1.5 billion in annual cost synergies derived from cost cutting and increased scale (purchasing and distribution). We believe the partnership's success in significantly boosting Heinz' margins provides a model for potential opportunities across the sector.

Hedge fund JANA Partners LLC (JANA Partners) revealed in a June 18 Schedule 13D filing that it had built a 7.2% stake in ConAgra Foods Inc. and that its performance disappointed following ConAgra's acquisition of private-label manufacturer Ralcorp Holdings in January 2013. JANA Partners is prepared to nominate three new directors to ConAgra's board and plans to engage management in discussions to improve shareholder value.

Potential activist opportunities

The presence of large, embedded shareholder interests can limit activist opportunities within the consumer staples sector. Companies with large shareholder ownership interests include Wal-Mart Stores Inc. (50% of shares owned by Walton family), Hormel Foods Corp. (49% by The Hormel Foundation), The Hershey Co. (7.9% class A and 99% class B shares by Hershey Trust Co.), Reynolds American Inc. (42% by British American Tobacco PLC), Boston Beer Co. (32% by C. James Koch), Kellogg Co. (20% by The W.K. Kellogg Foundation), Campbell Soup Co. (17% by Mary Alice Dorrance Malone), Keurig Green Mountain Inc. (16% by The Coca-Cola Co.), and Monster Beverage Corp. (17% by The Coca-Cola Co.).

Despite limited large-capitalization and mid-capitalization opportunities in the consumer staples sector, we believe The J.M. Smucker Co. ($13 billion market capitalization; Smucker's) may present an attractive opportunity to activist investors. The Smucker family continues to be highly represented in the company as it holds four of 13 board seats. However, the family's shareholder interest is limited with CEO Richard Smucker owning 2.4% and Chairman Timothy Smucker holding 1.9% of shares outstanding, which are considerably less compared with stronger embedded shareholder interests of the competing firms mentioned above.

Despite the June 2009 adoption of a shareholder rights plan (poison pill), allowing shareholders to buy shares at a discount if a non-Smucker family investor purchased more than 10% of shares outstanding, continued deterioration in operating fundamentals may set the stage for activists to win over other shareholders.

We believe Smucker's is attractive to activists given its sluggish top-line growth in the past five years (4.3% compound annual growth rate) that reflects healthy cash flows. Slow core product category growth for the company also echoes shifting consumer preferences toward healthier options found in store perimeters from the shelf stable, packaged goods the company offers in the center of the store.

Among this back-drop, Smucker's has experienced a significant deterioration in both its gross and operating margins in the past five years. Although the company has taken steps recently to accelerate earnings per share growth, with the March 2015 acquisition of Big Heart Pet Brands, we believe any integration miss-steps give activists opportunities to reverse significant share price underperformance of the past two years (up 5.6% versus a 29% rise in the S&P 500) and boost shareholder returns.

Table 2

Consumer Staples Investor Activism

Target/issuer	Announced date	Investor activist
ConAgra Foods Inc.	6/18/2015	JANA Partners LLC
The Coca-Cola Co.	6/17/2014	Wintergreen Advisers LLC
Mondelez International Inc.	10/30/2013	Trian Fund Management L.P.
Safeway Inc.	9/17/2013	JANA Partners LLC
PepsiCo Inc.	7/17/2013	Trian Fund Management L.P.
Herbalife International Inc.	2/14/2013	Icahn Capital L.P.
Herbalife International Inc.	1/11/2013	Pershing Square Capital Management
Clorox Co.	2/11/2011	Icahn Capital L.P.

Source: S&P Capital IQ.

--Joseph Agnese, S&P Capital IQ Equity Analyst

Energy

As a historically sleepy niche for investor activism, the energy sector has seen an increase of late. Between 2005 and 2009, S&P Capital IQ found just six cases of investor activism in the sector. In the subsequent six years, however, we noticed 34 instances of activist investors asking for change. Common demands in recent years include breaking up or spinning off a piece of an integrated oil company (i.e., Murphy Oil Corp. in 2012 and Hess Corp. in 2013). We believe a desire to separate the slower-growing refining businesses from the faster-growing upstream businesses motivated these activist inquiries.

Sector activism

Even within upstream, though, we have seen similar tactics (selling off less attractive businesses) to separate fast-growing reservoirs from slower-growing ones. Apache Corp. was a JANA Partners target in 2014 to sell off its international assets (slower growth) and focus its attention on U.S. shale plays (faster growth). Of course, JANA Partner's activist effort started in July 2014--before the crude oil price collapse from the former range of $90/barrel-$100/barrel to the current $60/barrel.

Because crude oil prices have seemingly stabilized at this new level and with the prospect that faster production growth is perhaps not as attractive as it once was, maybe it's time for some of the formerly fast-growing exploration and production (E&P) companies to consider an exit strategy. This subindustry is littered with highly leveraged firms that have seen their stock prices hammered. Furthermore, the longer the current price environment continues, the harder it may be for slow-growing companies to cope, particularly as fixed-price hedges expire.

Potential activist opportunities

We screened for U.S.-domiciled E&Ps trading on major U.S. exchanges with a number of key attributes to find key companies with activist opportunities. First, the company must have an average daily production of at least 100,000 barrels of oil to weed out the small names, which will likely not make a major impact on a possible suitor. Second, it must have a long-term debt-to-capital ratio of at least 50%, which suggests high leverage. And finally, its share price must decline by at least 30%. That screen returned three names: LINN Energy LLC and Continental Resources Inc., both of which S&P Capital IQ Equity Research does not cover, and SM Energy Co. ($3.1 billion market capitalization).

SM Energy Co.'s produced on average more than 150,000 barrels of oil equivalent per day in 2014. It has a long-term debt-to-capital ratio of almost 54%, and its stock price has dropped by about 40% during the past 12 months. SM Energy Co. has sizable production from south Texas, which is home to the Eagle Ford Shale and accounted for 73% of 2014 production.

There's no assurance, of course, that SM Energy Co. will receive a bid for its assets. Aside from being highly leveraged, SM Energy Co. will also likely generate a free cash flow deficit in 2016 that is wider than its peers' (relative to projected capital spending). It has a below-average reserve life, as well. In addition, while 55% of its expected 2016 production is liquids--on par with the 57% peer average--a sizable 25 of those 55 percentage points is anticipated to come from natural gas liquids (NGLs) with just 30 percentage points coming from crude oil. NGL pricing should remain weak through at least 2016, in our view, so realized pricing for SM Energy Co.'s liquid production may suffer relative to peers.

Table 3

Energy Investor Activism

Target/issuer	Announced date	Investor activist
Apache Corp.	7/22/2014	JANA Partners LLC
QEP Resources Inc.	10/21/2013	JANA Partners LLC
Hess Corp.	1/25/2013	Elliott Management Corp.
Murphy Oil Corp.	10/3/2012	Third Point LLC
Chesapeake Energy Corp.	5/25/2012	Icahn Capital

Source: S&P Capital IQ.

--Stewart Glickman, CFA, S&P Capital IQ Equity Analyst

Financials

Although a number of high-profile cases of investor activism have targeted Bank of New York Mellon Corp., Citigroup Inc., JPMorgan Chase & Co., and Hartford Financial Services Group Inc. (Hartford), some of these overtures proved unsuccessful for the activists. However, many of these target firms have taken notice and implemented a number of activist-initiated corporate governance changes.

The financial services sector faces a number of challenges in mounting a successful activist campaign. This space contains many large firms, so acquiring a 5% stake (and triggering a Schedule 13D filing) is difficult. Also, many of these firms are in highly regulated industries, such as banking and insurance, where implementing change requires regulatory approval.

Indeed, much of the recent activism has occurred in the less-regulated areas of the financial services sector, such as reinsurance (PartnerRe Ltd.) and REITs (Macerich Co.). Finally, we believe there is a degree of private activism as many of these firms have large institution investor bases that can agitate for change, particularly in board composition and executive pay.

Sector activism

Hedge fund investor John Paulson launched one of the most transformative activist campaigns against multiline insurer Hartford in 2012. Hartford suffered financial duress in the credit crisis and was forced to accept a government bailout. By early 2012, the company's shares were still trading at a deep discount to book value and were lagging its peers. On the company's fourth-quarter conference call in February 2012, Paulson publicly excoriated management and implored the company to "do something drastic" to boost its share price. By the following month, Hartford announced that it was planning to shut down its annuity operations and selling a number of noncore life insurance operations to focus on its more profitable property casualty and mutual fund units.

For its part, Hartford stated that an operations review was already underway when Paulson began to agitate for change. Still, Hartford's restructuring was broad-based and quickly executed. We believe Hartford attracted activist interest because its shares had lagged its peers' and were trading at a discount to book value. The company also had some legacy businesses that were underperforming.

We believe Genworth Financial Inc. has similar characteristics to Hartford. Genworth Financial Inc. is currently grappling with a number of underperforming business lines, and its shares are trading at 25% of book value (versus a peer group average of closer to 100%). Additionally, year-over-year through June 26, 2015, its shares have fallen 8.4% despite the S&P Multiline Insurance Index rising 8.6%.

We also expect activists' negative attention to be directed toward financial firms that still combine the chairman and CEO positions. This occurred recently when Bank of America Corp. extended the chairmanship role to CEO Brian Moynihan in the fall of 2014 and when JPMorgan Chase & Co. CEO James Dimon resisted calls to give up his chairmanship in the fall of 2014. Many U.S. banks combine the two roles, but we expect heavier pressure from activists opposed to this. In addition, because of populist backlash, many companies are giving up contributions to political action groups and think tanks, and we expect further activist pressure surrounding this issue.

Potential activist opportunities

Despite strong share price performance since the financial crisis, financial firms, such as American Express Co., Discover Financial Services Inc., T. Rowe Price Group, Franklin Resources Inc., Apollo Global Management LLC, Greenhill & Co., and Genworth Financial Inc. have underperformed in 2014 and 2015. For example, the loss of large card partnerships and a strong U.S. dollar that curtails foreign visitors to the U.S. have hurt American Express Co. Although American Express Co. is working hard to adjust its business to these two headwinds, we think the company will attract activist attention if problems persist for the next two years, which is generally the time span of underperformance that attracts activist attention.

Fellow credit card issuer Discover Financial Services Inc. has also underperformed versus the overall market because of the strong dollar and high marketing and rebate expenses. If these underachievements persist, we expect activists to push for wholesale changes. Asset managers T.Rowe Price Group and Franklin Resources Inc. have also lacked in performance, and we think they could become targets.

Bloated expenses and excessive restructuring charges also lure activists, though not that many glaring instances exist in financial stocks. One example was Bank of New York Mellon Corp., which attracted activist attention in 2014 due to a history of restructuring changes and a perception of wasteful spending. Similarly, State Street Corp. was also an activist target.

Finally, companies with large cash balances are often screened out by activists too. However, most financial firms are under formal regulatory capital regimes and often only return as much excess capital as they are allowed.

Table 4

Financials Investor Activism

Target/issuer	Announced date	Investor activist
Bank of New York Mellon Corp.	3/10/2015	Marcato Capital Management LLC
Aspen Insurance Holdings Ltd.	6/2/2014	Endurance Specialty Holdings Ltd.
JPMorgan Chase & Co.	4/10/2013	American Federation Of State, County, And Municipal Employees
Cincinnati Financial Corp.	3/15/2013	Miller Howard Investments Inc.
PNC Financial Services Group	3/14/2013	Boston Common Asset Management LLC
Citigroup Inc.	11/14/2012	Trillium Asset Management LLC
Chubb Corp.	3/15/2012	NorthStar Asset Management Inc.
Hartford Financial Services Group Inc.	2/14/2012	Paulson & Co. Inc.

Source: S&P Capital IQ.

--Cathy Seifert and Erik Oja, S&P Capital IQ Equity Analysts

Health Care

Based on S&P Capital IQ data, 52 investor activism transactions occurred from 2005 to mid-2015 within the health care sector, which ranks in the middle of the pack. We believe the number of activist investor-related activity within the health care sector has been somewhat muted in recent years as stocks performed remarkably well with the sector beating the broader S&P 500 composite index in each of the past four years.

Nonetheless, we believe activity could increase in the next year as some investors see opportunity because of significant sector changes because of regulatory or legislative issues, such as health care reform. As these changes provide opportunities within the sector, some companies will lag behind, creating opportunities for activist investors to push for strategic or management changes.

Sector activism

In 2013, hedge fund Glenview Capital Management (Glenview) disclosed that it had accumulated a 14.6% stake in Health Management Associates Inc., just below the 15% threshold that would trigger the company's poison pill. Glenview stated that it was evaluating its strategic options, including nominating a slate of directors, to replace the Health Management Associates Inc. board. Health Management Associates Inc. had experienced several quarters with many challenges, including financial underperformance, management turmoil, and a government subpoena regarding its billing and admission practices.

Shortly after Glenview's disclosed stake, Health Management Associates Inc. hired an investment bank to explore its strategic options, including a potential sale. In July 2013, the company received a takeover offer from Community Health Systems Inc. for $7.6 billion, including debt. In August 2013, Glenview won its proxy fight to replaced Health Management Associates Inc.'s entire board with eight independent directors, who subsequently agreed to the Community Health Systems Inc. deal, which was completed in January 2014 (Health Management Associates Inc.'s prior board had also agreed to the deal).

Potential activist opportunities

The recent Supreme Court ruling in the King v. Burwell case has removed the uncertainty surrounding the legality of tax subsidies and should continue to lower uncompensated care rates for hospitals and subsequently lift profitability.

Therefore, we see fundamentals improving, expect increased consolidation in the hospital industry, and believe opportunities will arise for activist investors.

Consolidation will increase scale, and thus we believe hospitals will gain improved operating and strategic leverage to obtain better pricing and contracts over supplies, such as pharmaceuticals, and reimbursements with health insurers. We believe Tenet Healthcare Corp., a leading national hospital chain, could be an attractive opportunity for investor activism. Tenet Healthcare Corp.'s stock performance has lagged behind its peers' in the past several years, and its EBITDA margins are well below its peers' at around 12% (compared with peers Community Health Systems Inc.'s 15% and HCA Holdings Inc.'s 20%). Glenview has a sizeable 13.9% stake in Tenet Healthcare Corp. as of February 2015.

Table 5

Health Care Investor Activism

Target/issuer	Announced date	Investor activist
Valeant Pharmaceuticals International Inc.	3/25/2015	Pershing Square Capital Management L.P.
Zoetis Inc.	11/2/2014	Pershing Square Capital Management L.P.
Amgen Inc.	10/21/2014	Third Point LLC
Alere Inc.	6/19/2014	Coppersmith Capital Management
Amedisys Inc.	2/3/2014	KKR & Co. L.P.
McKesson Corp.	7/1/2013	CtW Investment Group
Health Management Associates Inc.	6/25/2013	Glenview Capital Management

Source: S&P Capital IQ.

--Jeffrey Loo, CFA, S&P Capital IQ Equity Analyst

Industrials

The industrials sector has experienced notable activism with 51 announced actions in the past 10 1/2 years. Eight of these were announced recently, 14 were settled, seven were withdrawn, 11 were successful, and the remaining 11 were unsuccessful. Six of the total actions in the past 10 years have already taken place so far in 2015. But 2012 experienced the most activity with 13 attempted shareholder actions.

Sector activism

This sector has proven that not all investor activism leads to positive outcomes and increased share prices. Manitowoc Co. Inc., a long-time leader in the crane sector, became the subject of scrutiny from Icahn Capital L.P. in December 2014 after it purchased a commercial foodservice business. It was a leader in the refrigerated food business but had little in common with the crane business. Icahn announced that he had purchased a 7.8% stake in Manitowoc Co. Inc. and sought to have the two businesses separated, and he succeeded. In February 2015, Manitowoc Co. Inc. announced that it would split itself and would spin off the foodservice business by the end of 2015. It also offered Icahn seats on its own board, as well as on the new foodservice company's board. Since Icahn first disclosed a stake in Manitowoc Co. Inc. on Dec. 29, 2014, shares have fallen 12.6%, which proves that this piece of activism had a negative effect.

Car rental company Hertz Global Holdings Inc., which also came under scrutiny from Icahn in 2014, also experienced notable investor activism. In November 2014, Icahn had amassed a 10.8% stake in the company, had received several seats on the board of directors, and had a major say in the appointment of new CEO John Tague. From Aug. 20, 2014, when Icahn first announced a stake in the company to June 25, 2015, the company's stock fell 36%.

Potential activist opportunities

We think companies in this sector that may be underperforming financially, have illogical vertical integration, or have too many business units without cohesion become potential activist targets.

For example, Pitney Bowes Inc. is a leader in mailing; has a presence in e-commerce software and other digital technologies related to the mailing sector; sells mailing equipment; and outsources mailrooms and other mail services. The company's revenue has declines each year since 2001, and earnings per share have remained stagnant in the past decade as the company has sought to offset declining mail volumes with increased software and services revenues. The company represents ample opportunity for investor activism.

We expect the mailing business to experience a long-term secular decline while the software and e-commerce solutions business continues its growth of the past few years. We would argue that a potential activist could look to separate the mailing business from digital software to reignite the company.

The company also has a repurchase authorization in place to buy back up to $100 million in common stock, and we think an activist could try accelerating the pace of share buybacks.

Table 6

Industrials Investor Activism

Target/issuer	Announced date	Investor activist
Manitowoc co. Inc.	12/29/2014	Icahn Capital L.P.
The Brink's Co.	12/16/2014	GAMCO Investors
Hertz Global Holdings Inc.	10/10/2014	JANA Partners LLC
SPX Corp.	2/25/2013	Relational Investors LLC
The Greenbrier Cos. Inc.	11/13/2012	Icahn Capital L.P.
ADT Corp.	10/25/2012	Soros Fund Management
Navistar International Corp.	10/25/2012	GAMCO Investors
Canadian Pacific Railway Ltd.	12/1/2011	Pershing Square Capital L.P.

Source: S&P Capital IQ.

--Jim Corridore, S&P Capital IQ Equity Analyst

Information Technology

From 2005 to 2010, we surfaced only 11 examples of initiated investor activism in the information technology sector. But from 2011 through mid-year 2015, we identified nearly five times as much activity with 50 such actions.

We believe this elevated figure reflects greater sector acceptance of investor activism to develop positive changes for companies and stock performance.

In particular, we believe that from 2005 to 2010, technology companies were still dealing with the aftermath of the dot-com bubble bursting, considerable value loss, even discontinued operations (from 2000 into 2003), and the impacts from the Great Recession (2008-2009). We also think historically perceived complexities and high valuations of technology companies influenced investors away from activism.

More recently, we think value opportunities have become more apparent to some as many technology companies have experienced lower price-to-earnings (P/E) multiples or P/E-to-growth ratios than the S&P 500, as well as strong balance sheets with relatively limited leverage.

Sector activism

Instead of an "urge to merge," a major theme for technology companies in the past year or so has been something more akin to an "unrest to divest." In fact, four S&P 500 information technology companies--Computer Sciences Corp., eBay Inc., Hewlett-Packard Co., and Symantec Corp.--have each announced plans to split into two publicly traded companies by the end of 2015.

Interestingly, activists targeted two of the four companies prior to their break-up announcements: Computer Sciences Corp. by JANA Partners and eBay Inc. by Icahn Capital L.P. In 2011, Hewlett-Packard Co. added activist Ralph Whitworth of Relational Investors LLC to its board. And a few months ago, JANA Partners suggested Qualcomm Inc. separate its chip and licensing businesses, though management has stated it does not plan to do so.

In addition, we have noted activists have contributed to discussions about companies spinning off major stakes in other firms, including EMC Corp. and Yahoo! Inc. Earlier this year, Starboard Value L.P. prompted Yahoo! Inc. to spin off its interest in Alibaba Group Holding Ltd. Last year, EMC Corp. was pushed to do something similar by Elliott Management Corp. with its stake in VMware Inc., but it has resisted related action.

Potential activist opportunities

For our list of covered companies, we considered circumstances where disparate business segments are owned and operated, aren't strongly aligned, and aren't generating significant synergies--the most common in our coverage universe. Computer Sciences Corp., eBay Inc., Hewlett-Packard Co., and Symantec Corp. all have two major units largely because of acquisition activity. Activists were involved with three of these companies (excluding Symantec Corp.), and now all four of them are pursuing split-ups partly in response to perceptions associated with operational, financial, or stock underperformance.

Interestingly, Computer Sciences Corp. and Hewlett-Packard Co. are implementing divestitures involving services business with the latter splitting its hardware and software/services operations and the former separating its commercial and government operations.

We think it would make sense for Xerox Corp. (Xerox) to follow these companies and separate its document technology unit from its services operations. Although the company has a recognized brand and despite its marketing efforts, the company has surprisingly generated a majority of its revenues from services in the past few years after it acquired Affiliated Computer Services (ACS) for approximately $9 billion.

Although Xerox shares have risen 30% since it completed the ACS transaction, the S&P 500 Information Technology Sector Index has more than doubled during the same period. Xerox's normalized earnings per share, according to S&P Capital IQ, have slowly trended higher from $0.66 in 2010 to $0.74 in 2014, and revenues have declined in each of the past four years.

Xerox traded at a premium P/E to the information technology sector for most of the period from the beginning of 2010 to the middle of 2011; however, it has traded at a substantial discount ever since. We believe an activist could target the company to improve its focus and performance.

Additionally, we believe that EMC Corp. could still constitute an opportunity for activist investors because of its significant and valuable stake in VMWare Inc., which we see as undervalued. EMC Corp. shares have risen only 6.5%

since the beginning of 2013 compared with a 48% for the sector.

Table 7

Information Technology Investor Activism

Target/issuer	Announced date	Investor activist
Citrix Systems Inc.	6/11/2015	Elliott Management Corp.
Qualcomm Inc.	4/13/2015	JANA Partners LLC
Computer Sciences Corp.	2/23/2015	JANA Partners LLC
Yahoo! Inc.	9/26/2014	Starboard Value L.P.
eBay Inc.	1/22/2014	Icahn Capital L.P.
Apple Inc.	2/7/2013	GreenLight Capital Inc.
Yahoo! Inc.	9/8/2011	Third Point LLC
Motorola Solutions Inc.	11/30/2007	Icahn Capital L.P.

Source: S&P Capital IQ.

--Scott Kessler, S&P Capital IQ Equity Analyst

Materials

Investor activism in the materials sector has been more notable than we expected in the past 10 years given the sector's relatively small size. Activists have targeted companies that they believe they can increase shareholder value by instituting one or many corporate actions, such as cutting costs, initiating share buybacks, improving executive compensation structures, and divesting underperforming or slower-growth assets.

Across the materials sector, activist investors have used several tactics to achieve corporate action, especially requests for board representation, proxy contests, and takeover bids. Activists have achieved mixed results in their campaigns to enhance shareholder value in their holdings.

The materials sector has attracted 7% of total investor activism events in the past 10 years, twice the size of its 3.2% representation in the S&P 500 Index. Thirty-six different companies have experienced some form of investor activism with 32 cases occurring since 2010. About half of these actions were either a proxy fight or a threat to launch one, and 10 were shareholder proposals.

More than half of the actions were nonconfrontational communication and engagement with six of these leading to other actions, including shareholder proposals and proxy fights. Within the other 11 nonconfrontational communications and engagement actions, six are still considered, three were settled, and two were withdrawn.

Sector activism

One of the most public investor activism examples occurred in September 2014 when Trian Fund Management L.P. (Trian) launched a bid to force E. I. du Pont de Nemours and Co. (DuPont) to split into a growth company housing the agriculture, nutrition and health, and industrial biosciences businesses and into a cash/cyclical-oriented company housing the performance materials, safety and protection, and electronics and communications businesses. Arguing against the proposed split, DuPont said that it had delivered shareholder returns in excess of the S&P 500 since the end of 2008 by aggressively deploying leading science across the company, strengthening and fine-tuning its portfolio, and employing disciplined capital allocation. The company argued that these factors combined with the company's focus on cost control, its separation of the performance chemicals unit, and its share repurchase plans, showed that it is committed to building shareholder value. Trian then nominated four directors, including its founding partner Nelson Peltz, for election at the

2015 annual meeting. Trian lost the vote but obtained 46% of the votes.

In January 2014, Third Point LLC started an activist campaign against The Dow Chemical Co. by urging it to sell its upstream and downstream petrochemical businesses. The activists stated that the benefits from a spin-off would far outweigh the supposed integration benefits. Third Point LLC also pressed the company to increase its dividends and expand its share repurchase program. The company obliged and increased its dividends by 15% in early 2014 and 14% in early 2015. It also expanded its share repurchase program to $4.5 billion in January 2014 from $1.5 billion and then to $9.5 billion on Nov. 12, 2014. However, The Dow Chemical Co. said that Third Point LLC's proposal to split up the company showed a lack of understanding the company. On Nov. 21, 2014, the company announced an agreement with Third Point LLC to add four new independent directors to its board and to reduce the board size to 12. In return, Third Point LLC agreed to a one-year standstill and voting agreement.

Potential activist opportunities

Looking ahead, we believe that the close vote in DuPont recent proxy fight, in which a swing of nearly 30 million of the 698 million votes cast would have led to new board members, leaves the company vulnerable to future investor activism. Although the firm has had strong share performance in the past five years, we think its structure makes it a possible activist target. The company has seven main segments with only one segment having revenues greater than 30% of the 2014 total. Two additional segments have revenues that exceed 15%, and the remainder have 11% or less for each. The firm currently has $2.7 billion remaining in its current share repurchase program as of March 31, 2015, will likely see repurchase program extensions in our view, and has a 42% dividend payout ratio. Regardless, we think it is still a potential target.

Table 8

Materials Investor Activism

Target/issuer	Announced date	Investor activist
Owens-Illinois Inc.	12/17/2014	Atlantic Investment Management Inc.
E. I. Du Pont De Nemours And Co.	9/17/2014	Trian Fund Management L.P.
The Dow Chemical Co.	1/21/2014	Third Point LLC
Wausau Paper Corp.	10/22/2013	Starboard Value L.P.
Airgas Inc.	7/8/2013	Los Angeles County Employees' Retirement Association
Calgon Carbon Corp.	1/22/2013	Starboard Value L.P.

Source: S&P Capital IQ.

--Christopher B. Muir and Matthew Miller, CFA, S&P Capital IQ Equity Analysts

Telecommunication Services

The telecommunication services sector has experience extremely low activist interest in the past decade. We note that the highly regulatory nature of the space and limited growth prospects tend to steer activists clear from this sector. In addition, most telecommunication companies have highly leveraged balance sheets and low cash levels that further add to the unattractive nature of the space for activists. As a result, this sector has the second fewest levels of activist cases among the 10 sectors, and we view most of these instances as almost entirely devoted to corporate governance cases in nature.

Sector activism

Despite the lack of activism in the space, we have seen some attempts made in recent years.

GAMCO Investors Inc. (GAMCO) has made repeated efforts of late to urge shareholders to vote on its own slate of nominees to Telephone & Data Systems Inc.'s board of directors. Unfortunately for GAMCO, the company has been unsuccessful in every attempt. During the past decade, Verizon Communications Inc., AT&T Inc., and CenturyLink Inc. all experienced activist campaigns related to corporate governance issues (i.e., executive compensation, board member selection, etc.). However, none of these situations involved activists with significant holdings (more than 5%) with five cases being successful.

In April 2013, Maglan Capital L.P. (Maglan) launched an activist campaign against FairPoint Communications Inc. (FairPoint). Maglan stated that the company needed to find ways to improve shareholder value and proposed an annual cash dividend and selling FairPoint's Telecom Group assets. After numerous engagements between the parties, Maglan withdrew its campaign and converted into a passive investor in April 2014.

Although activists have largely stayed away from the sector, consolidation and M&A activity has been extremely active partially to increase economies of scale and to look for growth in a sector than offers relatively no growth. All four major wireless providers (AT&T, Verizon, Sprint, T-Mobile), as well as the local wireline providers, have been major participants in this trend. We believe the sector's high level of M&A may garner some sort of activist interest in the future.

Potential activist opportunities

We think Level 3 Communications Inc. (Level 3), a provider of fiber-based communications services, could be prone to activist interest for a number of reasons. First, we believe Southeastern Asset Management Inc. (Southeastern) could eventually become a more aggressive investor given its history. In the past, Southeastern has held activist roles in a number of its holdings, and its largest position is in Level 3 (12.8% stake at the end of first-quarter 2015). At the least, we expect Southeastern and Singapore-based Temasek Holdings Private Ltd., which together represent more than 30% of Level 3's holdings (as of the end of first-quarter 2015), will remain long-term investors and should support the share price.

We think Level 3 has the potential to generate significant free cash flow, potentially more than tripling in the next several years while capital spending increases modestly. We see increasing demand from customers given growing bandwidth demands, more complex mobile and cloud operating environments, and the need for global connectivity. Level 3 market share gain potential and large fiber network should allow the company to outgrow the industry and could make it a possible target in an industry witnessing significant consolidation, in our view.

Table 9

Telecommunication Services Investor Activism

Target/issuer	Announced date	Investor activist
Telephone & Data Systems Inc.	4/28/2015	GAMCO Investors
FairPoint Communications Inc.	4/11/2013	Maglan Capital L.P.
Verizon Communications Inc.	3/18/2013	Trillium Asset Management LLC

Source: S&P Capital IQ.

--Angelo Zino, CFA, S&P Capital IQ Equity Analyst

Utilities Sector

The utilities sector has seen little activist activity in the past 10 years. Because we believe this industry has been focused on shareholder return and spinning off or selling businesses after growing them, we think activist investors have had few incentives to get involved in the sector. In addition, utilities have been forming master limited partnerships from midstream assets and, in a new trend, forming "yield companies" from generating assets that have long-term contracts.

M&A activity within the sector, though muted in recent years compared with the late 90s and early 2000s, is still a significant source of value creation in the sector. We believe these moves within the sector have so far kept most of the activist investors uninterested.

There have been only six occurrences of investor activism in the past 10 years (two with the same company). Actions include shareholder proposals to split a company, director nominations, and rejection of proposed acquisitions. We do not think that there are any notable trends that would indicate a pickup in investor activism within the utility sector.

Sector activism

We believe there were two notable investor activist actions within the decade. One failed, and the other succeeded but eventually led to failure. In the first example, GAMCO, which owned 9.16% of National Fuel Gas Co. (NFG) in September 2014, instituted a proxy fight in April 2014 to spin off the company's utility into a separate publicly traded company. NFG argued that such a separation would lead to a loss of synergies and advised against voting for GAMCO's proposal. In March 2015, NFG reported that shareholders had voted against the proposal.

In a second example of shareholder activism, Seneca Capital Advisors LLC (Seneca) and Icahn Capital L.P. sought to block The Blackstone Group L.P.'s acquisition of Dynegy Inc. for $4.50 per share in cash because Icahn Capital L.P. argued that the deal wasn't enough. Dynegy Inc. argued that it didn't have enough cash to continue operations on its own for more than a year. After Seneca nominated its own slate of board members, Dynegy Inc. announced that the deal had increased to $5.00 per share in cash. However, shareholders dismissed the deal in November 2010. Then, Icahn Capital L.P. agreed to acquire Dynegy Inc. for $5.50 per share through a tender offer, putting it at odds with Seneca. Following a public campaign, shareholders failed to tender enough shares, leading to the CEO's resignation. By the end of 2011, Dynegy Inc. declared bankruptcy.

Potential activist opportunities

Looking ahead, we think Exelon Corp. could be ripe for some dose of investor activism. We note its dramatic stock price underperformance in the past five years compared with the S&P 500 Utilities Sector Index and its dividend cut to $0.31 per share quarterly from $0.525. We believe that activist investors may observe the separation of PPL Corp.'s unregulated generation assets from its utility business and think that they may see value in Exelon Corp. doing the same. Exelon Corp. has recently been focused on acquiring other regulated electric and gas distribution systems in an effort to capture merger savings and increase cash flows with the most recent acquisition of Baltimore Gas and Electric Co. driving the point home. Uncertainty surrounding the Environmental Protection Agency's treatment of carbon dioxide emissions from existing power plants makes ownership of unregulated natural gas and coal power plants risky, and the separation of those assets from the utilities could unlock the value of the utility businesses.

Table 10

Utilities Investor Activism

Target/issuer	Announced date	Investor activist
National Fuel Gas Co.	4/22/2014	GAMCO Investors Inc.
Dynegy Inc.	10/12/2010	Icahn Capital L.P.
Dynegy Inc.	1/14/2010	Seneca Capital Advisors LLC
National Fuel Gas Co.	9/12/2007	New Mountain Capital LLC

Source: S&P Capital IQ.

--Christopher B. Muir, S&P Capital IQ Equity Analyst

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