



Activist Insight

Monthly

BIG IS OVER



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ACTIVISM

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Monthly

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Small cap activism



An interview with Derek Bork of Thompson Hine and Waheed Hassan, CFA of Alliance Advisors.

[What's happening with activism at smaller companies? Is it increasing, and, if so, is that because of new entrants or established players?](#)

Waheed Hassan: Small cap companies, in particular those with market caps of \$1 billion or less, have been the primary target of activist investors for years. The emergence of “occasional” activists coupled with new activist hedge funds has further increased the number of small cap companies that are under attack.

Derek Bork: I see a couple of things developing as we work with activists in the small cap area. First, I think companies are responding to activists in a more organized fashion, but not necessarily a better fashion. I think companies are fighting back harder against activists, and I think this is most often a mistake. Second, I think companies are more willing to enter into a settlement with an activist, but I think this is most often motivated by an attempt to tie down the activist with a standstill and other entrenchment devices.

[What are the challenges for “knowing your activist” at this level, where executives may have less time and resources for monitoring their shareholders?](#)

WH: The biggest challenge is that many smaller companies lack the resources to understand activists. The company may not have the budget to engage a full-time investor relations officer, external consultants, or stock surveillance and

activist risk assessment programs, or participate in investor road shows. There are a myriad of tools available for shareholder monitoring that run the gamut from very affordable to prohibitively expensive and most small cap executives may have a difficult time assessing which tools would work best for them. All companies, especially small cap companies, should make the time to engage with at least their largest investors on a regular basis.

“Companies are fighting back harder against activists, and I think this is most often a mistake.”

[What defenses against activism are the least productive in this arena?](#)

DB: Although I think small cap companies are getting better at hiring advisors and preparing for a campaign, I do not think they are responding to campaigns any better. I think all too often companies are responding to activists in a disingenuous or hostile manner, and I think this is particularly true at small cap companies. Companies are more often managing an activist campaign as a legal battle instead of a shareholder relations matter.

WH: We saw a situation recently where, rather than working towards a mutually agreeable resolution during the proxy fight, the company chose to continue fighting and twice

rescheduled its annual meeting. The company rescheduled the meetings at the last minute, in our opinion, because they were losing the vote each time. This aggressive measure served only to upset their shareholders and cost them votes each time they pushed the meeting date back. The company's board may have been able to reach a resolution, but they instead lost control of the board.

[Is it relatively cheap to run a proxy contest at a small company, or are the costs somewhat fixed?](#)

DB: We develop budgets for our activist clients that make sure the total cost of the campaign, including the amounts spent on legal fees and proxy solicitor fees, makes sense in relation to the size of their investment. We work closely with proxy solicitors like Alliance to develop these budgets. We have gotten these budgets fairly low, and I think this is actually an advantage for our activist clients. Companies sometimes think they can gain an advantage by trying to run up the activist's costs, but I have not seen that strategy work.

[Do proxy voting advisers like ISS set a different standard for smaller companies, who might find reporting requirements more onerous?](#)

WH: As someone who managed the proxy contest research team at ISS, I can safely say that ISS's framework for evaluating proxy fights is the same regardless of company size. That said, small caps can have a lot more issues than their large cap peers –

“Retail investors – who often are pro-management – are not reluctant to support an activist when the targeted company has severe performance and governance issues.”

including with respect to share price, financial performance and corporate governance. Most importantly, small caps are generally not well prepared when they present their case to proxy advisory firms. Not surprisingly, at Alliance we spend a lot of time preparing our clients on how to engage with ISS.

DB: That advance preparation is especially important for activists that do not have a long track record of activism or board service. Newer activists should assemble their board slates and develop their case for change with the ISS framework in mind as a critical factor.

[How much information should either side in a proxy contest disclose to shareholders?](#)

DB: My advice is always to aim for full and fair disclosure. I think investors are more persuaded by arguments that are fair and well-reasoned. I think investors can easily spot misleading and unfair arguments, and I think it destroys credibility. I do not think that means you hold back the “dirt.” When something is fair game, you should share it with investors in a responsible way.

[How receptive to activist arguments are retail investors? Are there particular arguments they respond to?](#)

WH: Retail investors – while often pro-management in their voting tendencies – are not reluctant to support an activist when the targeted company has severe performance and governance issues. If a company’s share price has performed poorly or lagged its peers, or if there is a pay for performance disconnect, retail holders are likely to

side with the activist. That said, it is not easy to connect with a retail investor, especially Objecting Beneficial Owners (OBOs).

[What should activists know about targeting a small cap company?](#)

DB: How a small cap company will respond to an activist is often unpredictable. In the past, many companies have been unprepared, but today many companies are fighting back aggressively. Activists should prepare a strategy that takes into account all of the possible responses.

WH: Simply because a company is a small cap does not necessarily mean that they will be an easy target. In the past, many activists have failed to allocate sufficient resources, both of finance and time, because the target is a small cap and that cost them a victory.

[What’s the one thing smaller companies should know about activists?](#)

WH: Activists are in the business of making money. Before investing in any company an activist performs extensive research and in most cases has canvassed the shareholder base. Therefore, when an activist shows up as a shareholder, they are looking for a specific catalyst to drive up the share price.

DB: Companies should not think that an activist will be dissuaded by legal maneuvering or other tactics that a company might be advised to carry out. If an activist has launched a proxy contest, that means it has assessed the situation and is willing to fight all the way to the shareholder vote and even initiate litigation if necessary. [👇](#)

“Activists are in the business of making money.”

Waheed Hassan, CFA

Alliance Advisors

“Activists should prepare a strategy that takes into account all possible responses.”

Derek Bork

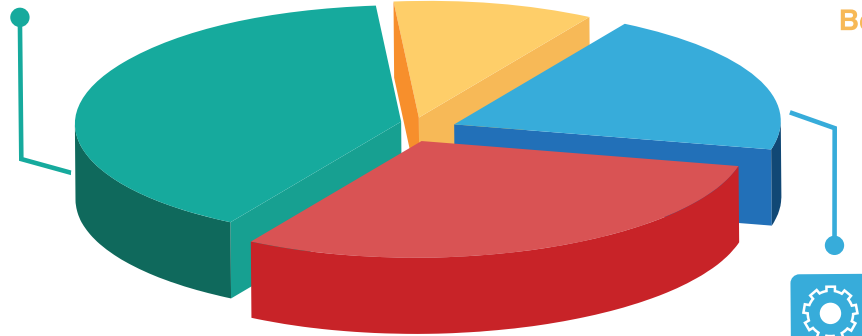
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Vertical Integration



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Most data is meaningless. Ours isn't.

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Leading Legal and Strategic Advisor for Small Cap Activism

Thompson Hine's activism group has a long and successful track record of assisting activist investors in achieving their objectives at small cap companies.

Our activist group was listed in the Intermediary Awards section of the December 2015 issue of *Activist Insight Monthly* for having represented activist investors in the fourth most campaigns during 2015 among all U.S. law firms.

Activist campaigns do not require daunting budgets. Our activist group is skilled at completing campaigns on budgets that are right-sized for small cap investments.



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