



## NAPF INVESTMENT CONFERENCE

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### ACTIVISM: THE DRIVERS FOR CHANGE

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#### INTRODUCTION

I am delighted to be speaking at this year's NAPF Investment Conference. It is a great privilege. The NAPF has made a tremendous contribution to shareholder activism. It will very much be in the driving seat going forward.

There's an important the distinction between investor activism and shareholder activism. We must be clear about it. The responsibility for being active lies with the owners – pension fund trustees – and their chosen investment managers. But it is the owners – the shareholders – who have the ultimate sanction. In the final analysis it is they who call the tune and pay the piper – or at least it should be. It's like having a dog. Do you want a rottweiler or a poodle as your investment manager? The choice is yours. But you must keep them on the leash. Some need a muzzle whereas others can be trusted to roam. But it is you – the pension fund trustees, the shareholders – who are in charge. You are the commanders-in-chief. But the investment managers – the commanders in the field – are responsible for execution and delivery.

#### ECONOMIC CONTEXT

The economic and market context for activism goes beyond Enron, Tyco and Parmalat. The context is critical to understanding the journey so far and the journey to come.

Let's look first at the dotcom bubble. Many dotcom companies had flaky corporate governance. We all have our scars: some went deeper than others. But the loss of investor

confidence as the bubble collapsed galvanised all to prevent any recurrence of the governance abuses.

But the bubble is now history. Markets have recovered their confidence and stability. But it is vital that investors and shareholders remain vigilant.

Second, pension fund deficits have sharpened attitudes to activism. The litany of statistics is familiar to us all. As a consequence, investment mandates are shifting away from relative performance to absolute performance. Away from balanced mandates to specialist mandates. Now this has particular relevance for activism, especially in a global context. Going forward, we, as fund managers, must take a similar activism approach for, say, Pacific Basin and North American portfolios as we do for our UK portfolios. Only by doing this will we deliver the exceptional returns which our clients deserve - and expect.

Third, the concentration of institutional power, especially in the 1990s. There is now no hiding place for the household names when it comes to activism. Commentators have rightly called into question how fund managers behave. It is inevitably entwined with the issue of trust. Fund managers worth their salt have to establish standards of conduct which demonstrate they take their responsibilities to heart.

Last, is the liberation of global capital flows, discerning in their pursuit of the best returns. This has caused governance gurus to look beyond their national boundaries. It exposed those economies, notably Japan and Europe, where shareholders have been inactive. These shareholders and investors have been asleep at the wheel. These economies have paid the price. Yesterday's leaders are today's laggards.

## DRIVERS OR CATALYSTS?

Let's now turn to the players. They are the catalysts for converting shareholder power into shareholder value. But sometimes the reactions can be explosive. One must handle with care!

### The Government

The Government has been an important catalyst. By commissioning Paul Myners and Sir Derek Higgs it has stimulated debate and provided a carrot and a stick to help ensure the desired reaction. The UK Government has given active investors many of the tools they need to be effective agents.

Yet we are still saddled with a company law structure that is crying out for reform. The Government is nibbling at the edges – albeit important ones – such as directors' and auditors' liability. The competitiveness of the British economy deserves a 21<sup>st</sup> century statute book. The Government should press ahead with this reform. The need for reform is as great today, if not greater, than it was 5 years ago.

### Institutional Shareholders' Committee

The ISC, which is the umbrella body for the NAPF, the ABI, the IMA and the AITC, made a major contribution with its statement on activism. True, several prods from the Government with a barbed fork were instrumental – not least to stave off legislation. The statement itself is a living document. Be under no illusions about that. It takes a good, commonsense approach. It reflects the views of practitioners. It is in touch with reality.

Trustees have a responsibility to read and understand this statement. It is not an optional extra. It is a benchmark for you as well as for your fund managers.

## **Investment Managers**

Fund managers can hunt individually or as a pack, as circumstances dictate. The NAPF's resuscitated case committees, which address specific activism situations, are an important development. They will lend authority to the discipline which pension funds bring to bear.

Much goes on behind the scenes. Most institutions are naturally disposed to this approach. It is generally effective. From time to time one has to go public but inflicting reputational damage on investee companies can be counter productive. But it is a tool of the trade. We have to be prepared to use it.

These meetings provide an excellent opportunity to encourage boards to make improvements to their corporate governance, not least strategy and management. Also, to hear how things look from their side of the fence. It just makes good sense.

## **Media Commentators**

Naming and shaming can be a potent catalyst. The cutting edge of comments from Anthony Hilton and his so-called 'competitors' can be sharp. As sharp as an executioner's blade.

They can challenge convention. They can expose practices which have become governance folklore. In doing this, they provide an invaluable service to one and all.

However, the quality of media reporting on activism is very variable. Sexed-up stories fuel an unhealthy frenzy.

But overall, the UK has been blessed with commentators who call a spade a spade and have advanced the causes of responsible activism and good governance.

With friends like these, who needs enemies!

## THE ROAD AHEAD

The acknowledged move from balanced to specialist investment mandates will have its implications for activism and corporate governance. It is worth noting that the ISC activism statement relates to all investments, whether they are in the UK or overseas. Going forward, to win these mandates and also specialist bond mandates, investment managers will have to demonstrate that they have the capability to take an active stance to enhance the value of their clients' investments.

I am pleased to announce today that Standard Life Investments is this year launching a Global Corporate Governance Platform, which will involve our portfolio managers, not just in Edinburgh but in Hong Kong, Boston and Montreal. We are building activism and governance into our global investment processes.

Regional Governance Co-ordinators have been appointed to provide local scrutiny and insights. Our global governance principles provide a strong foundation. They will ensure a consistent, principled approach is applied to all our clients' portfolios throughout the world.

We shall be raising our global game. The trend towards specialist mandates makes this a win-win proposition.

Trustees and their advisors are going to have to raise their game too. Paul Myners, Paul the Plumber, in his epistle to the Shareholder Voting Working Group, gave yet further encouragement to trustees to play their part. Trustees have to hold their fund managers to

account for how they behave. Voting is just the tip of the activism iceberg. Trustees must challenge their fund managers more regularly and more effectively.

The important role of advisors on activism must not be underestimated. Trustees will often look to them to provide a lead. They must help and inform Trustees. Advisers have to be active in their own way too.

Transparency and guidelines are also a key feature of the roadmap. Many large pension funds have their own activism and governance guidelines but many do not. Soon, those who do not will stand out like a sore thumb.

It is of course quite legitimate for pension funds, large or small, to adopt their fund managers' guidelines. These are our own guidelines, which I commend to you. A copy can be found on our website. These guidelines, which are applied with professional judgement, provide a basis of accountability for us to our clients. And to the companies we invest in. Without guidelines, investors will be like unguided missiles; more often than not, they will miss the target.

## CONCLUDING REMARKS

My nineteen year old elder daughter, Sallyann – one of the Jublets - has a passion for fashion. Successful fund managers have a passion for performance. But performance of itself in the field of activism and corporate governance is not enough. Our clients expect us to perform and to perform with integrity, as well as nurturing and encouraging the spirit of enterprise.

We take to heart our responsibilities as active investors.

Trustees, as active shareholders, must do so too. In the final analysis, actions must speak louder than words.