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Shareholder activism in South Africa: the directors' perspective

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ABSTRACT

Shareholder activism has become a dominant force in corporate activities today, and is a contentious topic in many corporate boardrooms. The purpose of this research is to provide a better understanding of shareholder activism in South Africa. The research achieves this by exploring the perspectives of company directors as they relate to the different aspects of shareholder activism and the impact thereof on South African corporates. The research furthermore seeks to establish directors' roles and responsibilities in dealing with shareholder activists, and the manner in which they believe they should prepare for and respond to shareholder activism.

A review of relevant literature shed some light onto various aspects of shareholder activism, including the key drivers, frequent demands and strategies commonly used by shareholder activists. In order to garner the desired perspectives, 15 semi-structured, in-depth interviews were conducted with the directors of listed companies across multiple industries. The study differentiated between executive and non-executive directors in terms of their roles and responsibilities in dealing with shareholder activists.

Four major themes emerged from the study, namely the type of shareholder prevalent in corporate governance activism, focusing on the firm's governance reforms; that there exists a level of optimism about the effectiveness of shareholder activism in corporate South Africa; the main activist type identified was the long-term institutional investor who prefers to engage directly with directors to resolve any shareholder related issues; and lastly, that most boards have strategies in place to effectively deal with shareholder activists.

This study revealed a void in academic literature in South Africa in terms of how directors should prepare for and respond to shareholder activism. This research attempted to address this shortcoming by using the empirical evidence to create and propose a guideline for directors, in order that they may prepare for and respond to shareholder activism in the future.

KEYWORDS

Shareholder activism, directors, corporate governance, shareholders

DECLARATION

I declare that this research project is my own work. It is submitted in partial fulfilment of the requirements for the degree of Master of Business Administration at the Gordon Institute of Business Science, University of Pretoria. It has not been submitted before for any degree or examination in any other university. I further declare that I have obtained the necessary authorisation and consent to carry out this research.

Name: _____

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Shareholder activism in South Africa: the directors' perspective

CHAPTER 1

1.1 INTRODUCTION TO THE RESEARCH

1.2 Research problem

Shareholder activism has become one of the powerful forces that institutions have to deal with in the modern day and a contentious topic in corporate boardrooms today (Goranova & Ryan, 2013). The rise of corporate scandals across the globe has resulted in frustrated shareholders seeking greater power to influence the actions of the companies in which they own stock. The influence that activists have on the market and corporates has increased. Furthermore, the level of shareholder activity is now ten times what it was during the 1990s (Black, 2015). According to a survey conducted by PricewaterhouseCoopers (PwC) in 2004 the United States of America (USA) alone had 343 activists' campaigns during 2014 – the highest number they have had since 2008.

The results of the 2013 proxy season by Proxy Pulse (2013) indicated a substantial increase in shareholder activism campaigns and a notable trend in activist activity in large corporations such as Apple, Pepsi, Dell, and JP Morgan Chase, among others. This is supported by the result of the Deloitte 2015, Quarter 1 signal survey, which reported that just less than three quarters of chief financial officers (CFOs) have experienced shareholder activism in one way or another. More than half of these CFOs say they had to implement a major business change in their respective businesses as a direct result of shareholder activism. A recent study by Ernst & Young (2011) revealed that 90% of corporate boards have shareholder activists impacting on their board agenda.

A study undertaken by (Greve, 2014) revealed that shareholder activism in South Africa – which can be attributed to an increasingly internationalised shareholder base in the country – is following global trends. A recent example of a last-minute counter-offer by Bidvest to frustrate Adcock Ingram's proposed R13 billion merger with CFR, a Chilean registered pharmaceuticals manufacturing and distribution company, is a case in point of shareholder activism (Bhuckory & Spillane, 2013)

Shareholders of companies listed on the Johannesburg Stock Exchange (JSE), such as Capitec, Massmart, Exarro and ArcelorMittal have begun to pay attention by voicing their opinions during annual general meetings (AGMs) on issues such as excessive pay

awarded to top executives and company remuneration policies inter alia (Crotty, 2015). The author also states that shareholders elsewhere in the country have started turning up the heat on companies' leadership on other issues, including corruption claims and Black Economic Empowerment (BEE).

A group of Woolworths Limited shareholders recently publicly criticised the retailer for buying some of its food items from Israel, demanding the retailer terminate its relationship with Israel until that country adhered to international human rights and rule of law (le Codeur, 2014). The activist group went on to further support a nationwide boycott at the retailer's stores to show their level of displeasure about the way the retailer was conducting its business.

Activists elsewhere in the world are also casting their eyes on South Africa. An international hedge fund holding 6,6% stake in AngloGold Ashanti Limited "put brakes" to the company's plan to raise US\$2,1 billion from investors and spin-off its South African operations (Mantshantsha, 2014). The activist shareholders agreed with the strategy of spinning off some assets, but was totally opposed to the way AngloGold was setting out to implement the strategy. They believed the planned implementation was value destructive for shareholders.

Recent legislative and regulatory changes have accelerated shareholder activism in South Africa. The introduction of the minorities' rights in the new Companies Act (2008) is likely to lead to increased activism in South Africa in the future (Hobson, 2010). The new Act sets out the framework within which shareholders can exercise their legal rights and pursue their agenda. According to the Act (2008), this can be achieved in two ways:

- In terms of section 61 of the Act, shareholders holding as little as 10% of total shares in issue can now call a general meeting under the Act; and
- The Act contains provisions that have elevated directors' accountability to shareholders to the extent that it is now easy for shareholders and stakeholders to institute legal action to directors and prescribed officers in the event that they suffered financial loss.

Some of provisions which afford additional rights to shareholders under the new Act include the following:

- Alternative dispute resolution ("ADR") (section 156 of the Act) – provides additional avenues to minority shareholders to resolve matters with directors.

This now includes Companies Tribunal, the High Court and the Takeover Regulation Panel;

- Protection of whistle blowers (section 159 of the Act) – affords minority shareholders protection for making certain disclosures about the company; and
- Application to declare a director to be delinquent (section 162 of the Act) – affords shareholders the right to remove directors that are not acting in the best interest of all the stakeholders.

The reduced threshold in terms of shareholding, widened scope in terms of who can bring a class action, and the right of directors to declare directors delinquent have resulted in the extension of liability for the directors under the new Act. This trend, according to Hannington (2012), means South Africa is likely to follow the same shareholder activism trends as countries like the UK, USA and Australia.

The scope of shareholder activism has increased substantially and many believe that it now plays an important role in shaping the corporate governance practices and performance in companies. A number of surveys conducted in and outside the country have demonstrated that there is a positive correlation between the performance of the company and good corporate governance. Shareholder activism has targeted corporate governance, as well as social, environmental and political issues (Dimitrov & Jain, 2011).

According to the King Code of Governance Principles - 2009 (King III), boards and directors, in their mandate to act in the best interests of the company, form a pivotal and critical point in corporate governance, with responsibilities extending to shareholders and all other stakeholders. The recent 2008 global financial crisis can be attributed to corporate governance failures. A number of corporate governance mechanisms, such as board monitoring, board accountability and risk management, failed to safeguard the interest of the shareholders, resulting in the crisis (Kirkpatrick, 2009). These shareholders, after losing a great deal of money in 2008, started looking at ways to safeguard their value (Brennan & Solomon, 2008).

The outcome of shareholder activism is not a homogenous practice (Adegbite, Amaeshi & Amao, 2010). Rather, it derives its identity from a host of heterogeneous factors and is, to a great extent, shaped by the actions of, or reactions to, and interplay among directors and shareholder activists (Goranova & Ryan, 2014).

1.3 Research objective

The purpose of this research is to explore the perspective of directors as it relates to an understanding of shareholder activism; the different aspects of shareholder activism; the impact of shareholder activism to South African firms; establishing their responses and responsibilities as key players in shareholder activism; and the manner in which they believe they should effectively prepare for shareholders' campaigns.

The researcher will meet the objectives mentioned above by conducting a critical review of shareholder activism literature, followed by practical research to compare the findings as presented in the academic literature with the perspectives of the directors.

Comparative shareholder activism research shows that there are different motivations for shareholder activism in different countries, supporting the importance of this study in light of the idiosyncrasies of each country (Adegbite, Amaeshi & Amao, 2010). Chung and Talaulicar (2010), also support the argument by stating national context as one of the variables in shareholder activism.

The choice of South Africa as a research country is not arbitrary for the following reasons:

- the country is at the forefront of corporate governance with the King reports on corporate governance having achieved international recognition status and having placed the country among the list of top custodians of good corporate governance;
- the increased shareholder rights and minority protection in the country;
- the country has well-developed financial market and fully functional stock exchange; and
- the country has undergone remarkable political changes since the advent of democracy in 1994.

Furthermore, most of the research on shareholder activism has been undertaken in the US, UK and Australia, with very limited research being undertaken in emerging markets. There has, however, been a steady increase in shareholder activism in emerging markets, particularly South Africa.

The research will contribute as a practical guide to assist directors and boards in dealing with shareholder activism. It will also contribute to academic research in shareholder

activism in developing countries. There has been limited comprehensive study research conducted on the role of corporate boards in shareholder activism and the range of actions available to them, which this research paper will endeavour to change.

Academic research reviewed on shareholder activism in the past mainly falls into two broad categories, namely:

- Antecedents of shareholder activism; and
- Impact or outcome of shareholder activism on corporates.

1.4 In summary

The literature review will demonstrate that managing shareholder activists and their demands is an imperative for corporates, more so in the last few years due to the changing business environment brought about by the 2008 global crisis, the change in the legislative framework brought about by the New Companies Act, 2008, and King III.

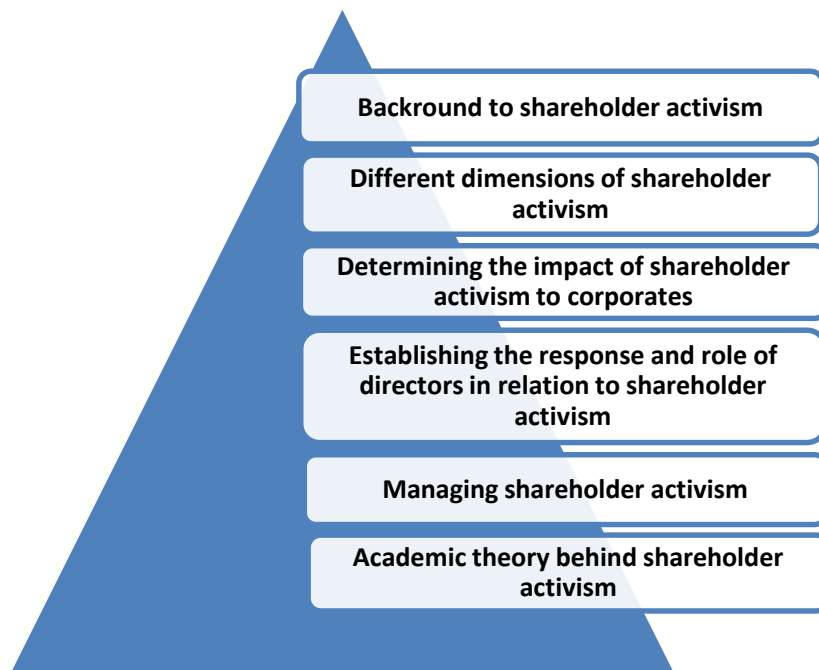
CHAPTER 2

THEORY AND LITERATURE REVIEW

2.1 Introduction

The literature review in this chapter will follow the diagrammatical representation set out in Figure 1 below. It commences with addressing the definition and background of shareholder activism. The literature is further reviewed to establish the different aspects of shareholder activism; the impact of shareholder activism on South African firms; establishing their responses and responsibilities as key players in shareholder activism; and the manner in which they believe they should effectively prepare for shareholder activists campaigns. The review will furthermore extend to the academic theory behind shareholder activism.

Figure 1: Diagrammatical representation of literature review



Source: Created by the researcher

2.2 Background to shareholder activism

Goranova and Ryan (2013), after reviewing relevant shareholder activism literature in recognised journals, summed up shareholder activism as actions taken by shareholders with the sole aim of influencing policies in corporations and not by seeking ownership of these corporations. Although shareholder activists seek to influence the companies they

target, it is not their intention to manage these companies or assume executive decision-making responsibilities. Shareholder activism is an enabling tool by shareholders to enforce rights and enhance value (Low, 2004). The definition of shareholder activism is very broad and accordingly accommodates a wide variety of actions. However, an end result by the activists is always to effect change.

Shareholder activism originated over 100 years ago as a feature of corporate governance (Rose & Sharman, 2013). However, it only really began to gain momentum in the early 1940s, when the USA's Securities and Exchange Commission (SEC) allowed shareholders to include issues in the form of proxy material to be presented in the annual general meeting.

Shareholder activism can be primarily differentiated into financial and stakeholder-centred social activism (Judge, Gaur & Muller-Kahle, 2010). This raises various debates around the weight that each stream carries, based on divergent theoretical foundations. Financial activism – also known as institutional activism – gained prominence in 1985 with the founding of Institutional Shareholder Services (ISS) and the Council of Institutional Investors (Goranova & Ryan, 2013).

Rose and Sharman (2013) identified two primary types of financial shareholder activism: firstly, performance-driven activism (advocating for an increase) in own wealth and secondly, corporate governance activism, focusing on the firm's governance reforms. The two are, however, not mutually exclusive. In some instances, corporations experience both, or the latter in order to achieve the former. Stakeholder-centred social activism normally revolves around social, religious or policy matters, and generally brings these issues and ideologies to corporate boardrooms.

This research proposal will examine financial activism which, according to Gillian and Starks (2007) has the highest impact on the outcome of the firm, as a form of shareholder activism. For that reason, any references to shareholder activism in the report will be to financial shareholder activism.

Some researchers, such as Gillian and Starks (2000), believe that shareholder activism arose due to a conflict of interest between managers and stockholders, while others, such as Smith (1996), argue that shareholder activism arises as an equilibrium condition when the expected benefit of activism exceeds the expected costs. In other words, shareholder activism is a 'numbers game'.

2.3 The shareholder activism landscape

2.3.1 Common types of shareholder activists

Shareholder activists, according to the PwC report (2015), have a wide spectrum, and the type of activism is based on the magnitude of the desired change that the shareholder would like to effect. Shareholder activism can take several forms. On the far end of the spectrum is hedge-fund activism, which asserts itself in achieving significant changes to the company's strategy, financial structure, management, or board (Cheffins & Armour, 2012). It is followed by 'vote no campaigns', shareholder proposals and, lastly, on the opposite side of the spectrum, 'say on pay' shareholder activism. Each of these will be discussed in turn.

2.3.1.1 Hedge-fund activism

Goranova and Ryan (2013) argued that although hedge-fund activists are late-comers in the field of activism, they are at top of the activist list in terms of assertiveness in desiring change in company strategy, structure and management or board. They have gained prominence very quickly due to the high monetary stakes involved. The modus operandi of hedge funders is to raise money from other investors to obtain large blocks of the company's shares, and thereafter to engage in proxy contests in the market for corporate influence (Cheffins & Armour, 2011).

Hedge-fund activists, unlike other activists, seek a quicker turnaround time in the implementation of their suggested changes. Researchers in the context of hedge-fund activism differentiate between offensive and defensive activism. Cheffins and Armour (2011) argued that hedge funds engage in offensive activism while the rest of the shareholders are more defensive.

Proponents of hedge-fund activism contest that it improves stock price and operational performance of the companies in which they are involved in the short-term, while critics argue that it reduces shareholders' wealth and may also result in the downgrading of certain stocks by increasing share-price volatility, as well as its debt structure (Brav, Jiang & Kim, 2009)

Critics of hedge-fund activism associate the phenomena with short-termism, a term used to describe the fact that this type of activism is associated with short-term gains at the expense of long-term gains in organisations. Bebchuk, Brav and Jiang (2013) opined that the reason researchers tend to argue short-termism is based on the fact that activists

tend to target non-performing and under-performing companies whose performance at the time of the activist activity was in a downward trend. Bebchuk et al. (2013) further argued that the period after the intervention is followed by improved corporate performance.

2.3.1.2 'Vote no' campaigns

The second type of shareholder activists are what researchers refer to as 'vote no' campaign activists. These activists coerce the other shareholders to withhold their votes from re-electing directors put forward by the board for nomination or appointment (Graves, Rehbein & Waddock, 2001). According to the PwC study (2015), vote no campaigns are ranked below hedge-fund activists in terms of assertiveness and ability to effect desired change in corporates. Ertimur, Muslu and Ferri (2011) added that 'vote no' campaigns are generally a defensive activism tool used by public pension funds.

Although there has been no conclusive evidence, empirical studies conducted suggest that most of the 'vote no' shareholder campaigns can be broadly categorised into campaigns for board best practice and for company-specific issues (Gladman, Grunfield and Lamb, 2012).

The most commonly cited best practice campaign relates to reasons such as "poison pill" approval without the shareholder consent, inadequate board attendance, related party transactions and directors sitting on too many boards (Ferris, Jagannathan, & Pritchard, 2003). The company-specific issues commonly cited are related to the remuneration policy and general shareholder dissatisfaction therewith.

2.3.1.3 Shareholder proposals

Another tool that shareholder activists use is the shareholder proposal, or the threat thereof. A shareholder proposal is formally submitted to a publicly traded company advocating for a specific course of action. Shareholders include their proposals in the proxies together with a statement explaining its opposition to be voted upon at the annual general meeting (Ertimur et al., 2011).

Thomas and Cotter (2007) highlighted four types of changes normally advocated by shareholder proposals, namely the changes are in terms of the board's governance policies, company's executive compensation, company's oversight of certain statutory functions, and the company's behaviour as a corporate citizen. According to Logsdon and Buren (2009), unlike hedge-fund and vote no campaign activism, shareholder

proposals are sponsored by a wide range of shareholders, including public pension funds, investment managers, hedge funds and individual investors.

Although shareholder proposals do not receive majority approval at board level, the number of proposals has steadily increased over recent years (Gillian & Starks, 2000). The type of sponsors and the type of proposals determines the success in terms of majority approvals. Gillian and Starks (2000) further argued that proposals sponsored by institutional investors and coordinated groups receive significantly higher votes than those sponsored by active individual investors commonly known as “gadflies”.

2.3.1.4 ‘Say on pay’ shareholder activism

‘Say on pay’ campaigns are considered by many investors as a more passive form of activism (Cai & Walking, 2011). ‘Say on pay’ activism is a result of the USA’s Dodd-Frank Act of 2010, which gave shareholders a say on the amount of remuneration that a company’s CEO and other executives would receive (ibid). The Dodd-Frank Act was promulgated immediately after the 2008 financial crisis to curb excessive executive pay levels and to attempt to link the pay levels to corporate performance.

While some researchers, such as Ertimur, et al (2011), argue that say on pay campaigns are becoming the most widely used tool to control executive pay, others believe the opposite is true, arguing instead that these campaigns are being used by boards to endorse the huge salaries currently paid to executives. In reality, say on pay activism is a tool used as a threat to force management and the board to critically review their remuneration policies and to link these policies to performance (Ferri, 2013). The fear of humiliation is working as a stick to curb executive remuneration. As with shareholder proposals, a wide range of shareholders participate in this type of activism, including individuals.

2.3.2 Key drivers of shareholder activism

The drivers of shareholder activism are varied, though Schneider and Ryan (2011) argued that most firms targeted by shareholder activists share certain broad similarities. Shareholder activism can result from the perception that a target firm has a low market value in comparison to its book value and is in a poor-performing industry (Opler & Sokobin, 1997). Karpoff (2001) argued that although these firms have low market value in poor-performing industries, they are not necessarily the worst performers in that industry. In fact, Klein and Zur (2009) pointed out that shareholder activists tend to target

more profitable firms. Smith (1996) found no significant difference in the market value to book value between targeted firms and non-targeted firms. Karpoff (2001), and Black (1997) found that firms targeted by shareholder activists have low sales growth, with Bizjak and Marquette (2008) adding the low operating income growth factor to this equation. Karpoff (2001) also found that targeted firms are highly geared as compared to non-targeted firms. Furthermore, firms targeted by hedge funders have high institutional ownership and tend to be large in size – facts agreed upon by most researchers.

Another factor driving shareholder activism, identified by PwC (2015), is the board that does not meet best practice expectations and which has a different governance profile to that of its peers. Examples of this include board compositions and the length that board members have served on boards, among other things.

Other qualitative factors identified that drive shareholder activism can be summarised as following:

- A company that has a majority shareholder proposal that has not yet been implemented (Lipton & Lorsch, 1992).
- A company that has previously received a ‘vote no’ campaign or a request to remove one of its directors (ibid).
- A company that has received media or public criticism in relation to a policy or a decision made by the directors (ibid).
- A company in the market for a new CEO (Bebchuk, et al ,2013).
- A company with an inefficient capital structure (Mallin, Mullineux & Wihlborg, 2005).
- A company failing to adapt to certain financial conditions (ibid).

According to Mallin et al. (2005), shareholders’ activism campaigns are prevalent in poor-performing companies. This has, however, changed since the financial crisis of 2008, as shareholder activists are now looking for flaws in corporate governance to protect the value of their investments. Moreover, they are increasingly holding firms to account. In recent years, technology has also led to increased shareholder activism through better communication and different and efficient media platforms (ibid).

2.3.3 Demands commonly made by activists

Shareholder activists' demands are often related to the strategic direction of the company involved (Judge & Gaur, 2010). Gantchev (2013) summarised the most common demands made by activist shareholders to corporates into the following three categories:

- The first category pertains to corporate governance-related demands. Included here are election of shareholder activist nominees to the board of directors, the removal of certain board members, and the replacement of management. Executive remuneration and additional disclosure requirements also fall within this category (Gantchev, 2013).
- The second category of demands usually pertain to the company's capital structure (Klein & Zur, 2009). This includes dividends, debt restructuring and companies' recapitalisation. Hedge funds are known to address agency costs related to cashflow, whereas other shareholder activists or investors seek to change the investment strategies of the target companies. A more aggressive type of demand is divestiture and/or sale of significant parts of the business. Liquidation of a company and the declaration of a special dividend also fall under this category. These types of actions enhance value and secure higher payouts to shareholders (Ganchev, 2013).
- The third category relates to strategy, as shareholder activists often criticise operational inefficiencies and unprofitable businesses. They also recommend strategic initiatives to improve underperforming businesses (Schneider & Ryan, 2011).

2.3.4 Strategies used by shareholder activists to realise their demands.

According to PwC (2015), shareholder tactics are evolving. The strategies used by activists fall along a spectrum based on the type of change and the significance of the desired change. Brav, et., al, (2009) confirmed that some of the examples of the strategies used by activists include requesting a meeting with management or leadership; appealing to directors using media campaigns; behaving aggressively at shareholder meetings; opposing strategic or merger and acquisition plans; and litigating to prevent company actions or to override company rules.

Many shareholder activists make an effort to talk to companies in a bid to reach a consensus around intended changes before pursuing other tactics, such as media campaigns, proxy and litigation. Furthermore, shareholder activists often test the waters

with other shareholders in order to gauge their receptivity to the planned changes or strategies (Girard, 2011). Some of the most persuasive strategies used by shareholder activists are lobbying of other shareholders and using the media to achieve their objectives (ibid).

2.4 Impacts of shareholder activism

2.4.1 Positive aspects of shareholder activism

To date, numerous studies have highlighted the benefits of shareholder activism, which can be broadly divided into three main categories; namely, the creation of wealth for all the shareholders; the improvement in corporate governance; and the enhancement of management skills and knowledge in the organisation. Each of these will be discussed in turn below.

2.4.1.1 The creation of wealth for all shareholders

Bebchuk et al., (2013) in their study of the long-term effects of hedge-fund activism, found that shareholder activists' interventions are beneficial to the company, both in the short and long-term. Bechuk et al. (2013) were disproving the theory that activists reduce the amount of capital in the companies required for future expansion and growth.) Cohn and Rajan (2013) added that another way shareholder activists create value is by ensuring that transactions entered into by the companies are entered at fair market value to avoid arm's length transactions that seek to destroy value for the shareholders. This was highlighted in the case of Michael Dell of Dell Computers, who tried to privatise the company at a price lower than fair market value at the time.

2.4.1.2 Improvement in corporate governance

Smith (1996) found that, overall, shareholder activism has a positive effect on corporate governance structures. He added that activists have been successful in getting their desired governance-related changes adopted in cooperatives. This is particularly true for performance-related changes and the removal of ineffective directors (Ertimur et al., 2011; Smith, 1996). According to Ernst & Young (2012), activists, while safeguarding their interests, also protect the interests of other shareholders.

Shareholder activism by hedge funds became a major corporate governance occurrence in the USA during the 21st century. Despite the financial crisis of 2008, the hedge funds

involvement has remained an important element of the country's corporate governance strategy going forward.

Shareholder activism improves transparency in organisations (Bushman & Smith, 2003). In fact, the definition of corporate governance is grounded in transparency. Transparency can be described as:

- The promotion of disclosure in companies and the empowering of minority shareholders regarding their rights to the information environment (ibid);
- The enhancement of accountability in companies and protection of the rights of all company stakeholders (Clarke, 2004); and
- A tool to equalise the information available to all stakeholders (Botright, 2002).

Their findings showed that institutional investors call for meetings with company managers to discuss strategic initiatives on a regular basis and are involved in activities to promote corporate governance standards and accountability (Martin & Nisar, 2007). Furthermore, they analyse information concerning the companies in which they have invested in on a regular basis.

2.4.1.3 Enhancement of management skills and knowledge in the organisation

Shareholder activists target non-performing firms or under-performing firms with the aim of turning them around (PwC, 2015). The turnaround of these firms requires skills that management does not necessarily possess – otherwise they would have done so without the help or assistance of expert advice from shareholder activists. Institutional investors have specific capabilities for monitoring and controlling portfolio companies (Martin and Nisar, 2007).

2.4.2 Negative aspects of shareholder activism

Research on shareholder activism offers conflicting perspectives on shareholder engagement. There are nearly as many proponents of shareholder activism as there are detractors. One of the principal criticisms of shareholder activism is that activists concentrate on the short-term gains at the expense of long-term interest. A survey undertaken by Morgan Stanley in 2012 revealed that the time horizon of some of these activists is as short as three months, with only 20% taking as long as a year. Karpoff (2001) agreed that shareholder activists have a tendency to focus on short-term metrics rather than building long-term shareholder value. Bechchuk et al. (2013), however,

argued that interventions by shareholder activists do not adversely affect the long-term value of the company.

Shareholder activists have been termed 'bullies' due to the fact that they deploy campaigns which result in distracting management from performing their duties, leading to impaired company performance. According to Karpoff (2001), shareholder activists rarely have the skills and the experience to steer companies in the right direction and are therefore unlikely to add value or improve managers' decisions.

Yet another view is that shareholders may, in some instances, pursue goals that do not seek to maximise value for the company and other shareholders (Karpoff, 2001, p. 7). Examples include when activist shareholders pursue politically motivated or social objectives associated with decline in the value of a company.

2.5 Boards' responses to shareholder activism

According to Hoffman (1996), there are three factors that determine a company's response to shareholder activism; namely, the political climate in which the firm operates; the culture of the firm; and the power and influence of the shareholder activist group. Furthermore, the way a company responds to shareholder activism forms part of its strategy.

Reviewed literature does not provide much guidance on the types of responses available to companies when corporate activists knock on their door. Indeed, company directors have many decisions to make in their responses to activism. According to Cossin and Caballero (2013), these responses can be classified into three typical reactions. The first, companies can react proactively by engaging with shareholder activists by acquiescing to their requests, which normally results in the withdrawal of the shareholder activists' demands due to the companies conceding to comply with these changes. The second, some firms react defensively by rejecting shareholder requests, which often prompts the involvement of all shareholders in a form of proxies. This is where shareholder activists normally deploy the tactics listed under **section 2.5** to achieve their objectives. And finally, companies can collaborate and compromise with activists. The benefits of engaging activists in a direct dialogue are an indication that the company is taking seriously the concerns of its critics, and opens doors for mutual understanding of transfer of expertise from both parties (Rehbein, Logsdon & Buren (2013)).

2.6 Preparation for shareholder activism

As shareholder activism gains prominence in many organisations, so the question needs to be asked regarding the steps that management should take to prepare for their demands, and strategies they could use to limit the potential impact of the phenomena. However, there is limited research available on how companies prepare for shareholder activism. In fact, the only literature available is from professional papers written and published by subject matter experts. This sub-heading is, however, very relevant to the objective of the research topic and needs to be included in the literature review.

Despite the growing strength of activist shareholders, companies can take a number of steps to effectively prepare for, and respond to, activist campaigns (PwC, 2015). First, company directors must critically evaluate the business and look for attributes that put the company at risk of being targeted. Some of the red flags as identified by Atkins (2013) include financial underperformance by the company, excess cash in the balance sheet, and a reduction in the company's market capitalisation. Secondly, the company needs to monitor and understand the shareholder base and understand the shareholders and their priorities (Atkins, 2013).

There are different types of shareholder activists as discussed under section 2.2 and, according to the PwC report (2015), as part of their preparation, companies need to understand the type of demands these shareholders are likely to raise.

Lastly, companies need to adhere to principles of good governance (Cohn & Rajan, 2013). According to Martin and Nisar (2007), companies with a track record of good corporate governance are likely to gain support of institutional investors who, in most instances, are the largest shareholder body. It then becomes easier to deal with other shareholder activists. Atkins (2013) opined that the most effective early-warning system for companies in terms of dealing with shareholder activists is keeping their ears on the ground.

2.7 Academic theories behind shareholder activism

The primary goal of a theory in research is to answer the questions about the research of when, how and why (Bacharach, 1989). A primary concern here is to identify theory's ability to explain the shareholder-director relationship. The theoretical framework of shareholder activism is directly linked to agency theory, theory of corporate governance, and stewardship theory.

2.7.1 Agency theory and shareholder activism

The justification for shareholder activism is to resolve the agency conflicts inherent in organisations (Gillian & Starks, 1999). Hence, agency theory is the most dominant theory in shareholder activism (Daily et al., 2003). It is also the most invoked (Goranova et al., 2013).

Shareholders, by virtue of the fact that they are the owners of capital, delegate their decision-making responsibility to managers or directors who do not have the incentives to make decisions in the best interest of the shareholders (Gillian & Starks, 1999). Agency theory is based on the premise that managers are narcissistic and do not carry the full risk of their corporate decisions (Eisenhardt, 1989).

The theory attempts to solve two specific problems, namely, alignment of the principal's goals to prevent conflict between principal and agent, and alignment of the risk tolerance of the principal and the agent (Eisenhardt, 1989). Simply put, in agency theory, the principal delegates to an agent (who is looking after his/her interest) to do the work.

Agency theory works on the premise that there is conflict of interest between principals and agents. Eisenhardt (1989) further argued that, in an imperfect market, agents will always seek to maximise their own gains at the expense of shareholders. This is based on the fact that agents, who are managers of the firms, have more information at their disposal regarding the firm than do the shareholders.

Shareholders recognise that the firm will make decisions not in their best interests and have invoked agency theory to conceptualise the monitoring of managers. Daily and Canella (2003) argued that shareholder activism is one of the agency theoretical principles that is instructive on the subject of corporate practice. They further stated that shareholder activism is designed to reduce managers' self-interest by coercing managers with incentives to implement practices that safeguard shareholders' interests.

Agency theory, in practice, does not guarantee increased shareholder wealth but rather, ensures that managers will apply any means possible to attain favourable outcomes for shareholders (Davis, Schoorman & Donaldson, 1997). According to Daily and Canella (2003), agency theory is a very popular concept in corporate governance research and dominates corporate practice due to its simplicity and the notion of human self-interest and rationality. The major criticism of the theory is its simplicity, which stems from the fact that it reduces the number of participants in corporations to two, namely, managers

and shareholders. Shareholders' activism is a very instructive tool in terms of corporate governance. The governance transformations pursued by shareholder activists seek to shed some light into valid and effective governance practices of protecting shareholder interests (Daily & Canella, 2003, p. 373).

2.7.2 Stewardship theory and shareholder activism

In reality, agency theory may not apply to all manager-principal situations. An alternative to agency theory is stewardship theory, a relatively new theory that defines situations in which owners and managers' objectives are aligned and managers are not motivated by individual goals (Davis, Schoorman & Donaldson, 1997). In terms of stewardship, there exists manager-principal interest convergence.

The theory is based on the model of man, the behaviour of which is pro-organisational and collectivistic and will unlikely depart from the interest of the organisation (Davis et al., 1997, p. 24). This behaviour is based on the premise that if shareholder wealth is maximised, then the steward's utility functions are also maximised, which implies a strong relationship between the organisational success and that of its principal. Stewards, in most cases, are motivated to maximise organisational goals as well as those of shareholders and other stakeholders.

In terms of stewardship theory, the steward recognises that there is trade-off between personal needs and organisational objectives. The theory states that in working towards organisational needs, personal needs are met (Ibid, p. 21). The proponents of stewardship theory have in no way adopted the view that the executive managers are noble in their dealings with the principals, but recognise that they are situations where managers serve shareholder interest because by doing so they are also serving their own interest (Daily & Canella, 2003).

2.7.3 Agency and stewardship theories: complementary and contradictory factors

The one side of the argument is, given the benefits of stewardship theory to both shareholders and the organisation, it is unclear why shareholders or principals still opt for an agency relationship rather than a stewardship relationship. According to Davis, et al (1997), the risks that shareholders are willing to assume determine the governance contract between shareholders and the managers of the businesses. The risk orientation of the shareholder plays a critical part in determining the management philosophy of the organisation.

Empirical evidence shows that risk-averse shareholders are comfortable with the principal agent relationship in order to insulate themselves from managerial self-interests. Applying the McGregor's X and Y theory of motivation, the agency relationship is governed by the principles of theory X. The opposing side of the argument is that, given the conflict of interest between the shareholders and executives, why would shareholders take the risks on the stewardship governance structure?

Stewardship theory is viewed as both complementary and contradictory to agency theory; there are conditions under which each is necessary. Davis et al. (1997) attempted to find the appropriate use of one theory to complement the other in corporate governance, rather than try and prove which theory best serves the shareholder and the organisation. There are psychological and situational factors that influence shareholders and managers to pursue either agency or stewardship relationships (Davis et al., 1997).

Table 1: Comparison of agency theory and stewardship theory

	Agency Theory	Stewardship Theory
Model of Man	Economic man	Self-actualising man
Behaviour	Self-service	Collective serving
Psychological mechanisms		
Motivation	Lower order/economic needs (physiological, security, economic)	Higher order needs (growth, achievement, self-actualisation)
	Extrinsic	Intrinsic
Social comparison	Other managers	Principal
Identification	Low-value commitment	High-value commitment
Power	Institutional (legitimate, coercive, reward)	Personal (expert, referent)
Situational Mechanisms		
Management Philosophy	Control oriented	Involvement oriented
Risk orientation	Control mechanisms	Trust
Time frame	Short-term	Long-term
Objective	Cost control	Performance enhancement
Cultural differences	Individualism	Collectivism
	High power distance	Low power distance

Source: Davis, Schoorman and Donaldson (1997) Page 37

The choice between agency and stewardship theory has an impact on shareholder activism and corporate governance. Faly (2006) defined corporate governance as procedures implemented by organisations with the aim of directing and controlling an organisation to maximise shareholder value. Financial activism, as part of corporate governance strategy, addresses the agency conflict at the core of public firms (Gillian & Starks, 2007). Social activism pressures companies to change their practices, resulting in a change in social impact (Sjostrom, 2008).

Cornelius (2005) defined corporate governance as a stewardship responsibility of directors to oversee the objectives, assets and strategies of a corporate and to ensure that these requirements are implemented. Stewardship theory explains that managers, left on their own, will act responsibly towards the assets they control, therefore minimising the need for activism on the part of shareholders.

The choice between agency and stewardship theory is a mutual decision in the agent and principal relationship. There are numerous possible choices from which each party can choose. Davis et al. (1997) compared the decision to be made by parties to a decision posed by a prisoner’s dilemma. The impact of the choices is illustrated below in a model called the principal-manager choice model.

Table 2: Principal-manager choice model

		Principal’s Choice	
		Agent	Steward
Manager’s Choice	Agent	Minimise Potential Costs Mutual Agency Relationship Quadrant 1	Agent Acts Opportunistically Principal is angry Principal is betrayed 2 Quadrant
	Steward	Principal Acts Opportunistically Manager is Frustrated Manager is Betrayed Quadrant 3	Maximise potential Performance Mutual Stewardship Relationship 4 Quadrant

Source: Davis, Schoorman and Donaldson (1997) Page 39

The choice of position of the parties depends on the level of risk acceptable to each individual and his propensity to trust the other party (Davis et al., 1997). In this dilemma, the parties find themselves with four possible situations, as outlined below.

Quadrant 1 – Mutual principal-agent relationship: This results in a low risk of betrayal and the mechanisms are put in place by the principal to monitor the agent's behaviour. Costs are controlled.

Quadrant 4 – Mutual stewardship relationship: This results in trust relationship. The principal invests in an involvement-oriented and empowering situation. Mutual gains are maximised.

Quadrant 2 and 3: The dilemma occurs when the choice of the parties diverges. This happens when the principal decides to act like a steward while the manager decides to act like an agent. In the situation where the manager acts opportunistically and takes advantage of the empowered relationship, the principal feels betrayed and frustrated. This normally results in the principal implementing more stringent monitoring controls and withdrawing empowerment. Conversely, in a situation where the principal acts opportunistically, the manager is unlikely to enjoy the benefits that come from stewardship relationship such as growth, sense of achievement and self-actualisation. The cost of disenfranchised managers for any organisations is very high.

2.10 Conclusion

The academic literature review indicated that various components of shareholder activism have been researched with varying depths and intensities. Several areas were supported strongly by literature, while clear gaps were present in others, most notably in the strategies used by shareholder activists to realise their demands and the various ways in which boards and companies prepare themselves for shareholder activism.

Accordingly, opportunities existed for the researcher to test the areas addressed by the literature and to supplement areas not adequately addressed. The researcher sought to supplement the literature by reviewing professional literature prepared by subject matter experts in the industry. The academic literature review furthermore highlights the landscape of shareholder activism. The clear corroboration in the literature is sufficient to advocate the need for boards to manage shareholder relationships and shareholder activism.

In conclusion, understanding the landscape and nuances of these relationships is critical for the board when developing a strategy for dealing with shareholder activism.

CHAPTER 3

RESEARCH QUESTIONS

The research objectives set out in Chapter 1 centred on analysing directors' perceptions as they relate to shareholder activism in South Africa. Accordingly, the following research questions are posed:

3.1 In order to understand shareholder activism, an acceptable definition is required, as follows:

Research question 1: What is shareholder activism in the context of South African firms?

3.2 Clarity must be provided about the different players in the shareholder activism space, as follows:

Research question 2: Who are the shareholder activists in South Africa?

3.3 In order to substantiate the importance of shareholder activism, its impact to companies must be explored, as follows:

Research question 3: What has been the impact of shareholder activism on South African companies?

3.4 In order to understand the relationship between different elements that make up shareholder activism and to understand the most important ones, key drivers must be identified, as follows:

Research question 4: What are the key drivers of shareholder activism in South Africa?

3.5 In order to manage the impact of shareholder activism in companies, the most common demand made by the activists must be understood, as follows:

Research question 5: What are the common demands made by shareholder activists in South Africa?

3.6 In order to gain insight and examine discourse the responses of the collective must be understood, as follows:

Research question 6: What are some common strategies used by activists to realise their demands?

3.7 In order to understand the behaviour of the boards towards shareholder activism as follows:

Research question 7: How do South African boards respond to shareholder activism?

3.8 In order to understand the framework within which directors can operate the role of corporate boards must be understood, as follows:

Research question 8: What is the role of corporate boards in dealing with shareholder activists?

3.9 The research culminated with the final research question, as follows:

Research question 9: How do corporate boards prepare for shareholder activism?

CHAPTER 4

RESEARCH METHODOLOGY

4.1 Research methodology

The process of devising a research methodology and strategies to build a theoretical framework is to confirm that the research topic is a subject of management research (Jain & Narvekar, 2004). In order to conduct the research and answer the research questions presented in Chapter 3, the research process used an inductive strategy. The reason for choosing an inductive approach was to look at shareholder activism phenomena from a different perspective. This approach also enabled the researcher to adopt an open approach in terms of what the research may reveal.

4.2 Research design

Three types of research studies were used in the research design, namely exploratory, descriptive and explanatory (Saunders & Lewis, 2012). A brief explanation of each follows:

- Exploratory research – used to gain new insight into a new topic or an assessment of an existing topic in a new light.
- Descriptive research – used to accurately describe a situation without necessarily analysing it.
- Explanatory research – uses descriptive research to discover and explain causal relationships between key variables.

The aim of the study was to gain an insight into how the directors perceive and respond to shareholder activism in South Africa. Saunders and Lewis (2012) recommend an exploratory study when new insights are sought in terms of a topic. This helped to assess an existing topic in a new light. Exploratory research furthermore assisted the researcher to find clarification on several questions. It also afforded the researcher an opportunity to understand the research subjects' environment, which is invaluable to the research.

As the research aim was exploratory, a qualitative research methodology was employed as the primary research approach. Denzin and Lincoln (2000) describe qualitative research as a research methodology that look for answers to questions; uses a predefined set of procedures and methods to answer the questions in a logical manner;

produces findings that were not pre-determined; collects evidence and produces findings that are can be applied further beyond the study requirements.

Some of the exploratory qualitative research methodology that is been most useful in meeting the researcher's objective are:

- The study seeks to explore a particular phenomenon;
- The instruments and study design used in the study are flexible and iterative - data collection and research questions are modified to the learnings;
- The method can be used to describe individual experiences; and
- The questions are open-ended.

The study to get new insight into the perception of directors to shareholder activism phenomena, which made the method an appropriate method to use.

Although exploratory research method provides insight into the topic and issues being researched, it is in no way a conclusive or definite research methodology (Saunders & Lewis, 2012).

4.3 Generating primary data

The research mainly used primary data. The reasons for the use of primary data include that the data was collected from the field by the researcher, and that the data is useful for current as well as future studies. Where secondary data was available, comparison was made to the primary data. Once validity and accuracy had been established, the secondary data was used to augment the primary data.

4.4 Data collection

The three most common methods of collecting data for qualitative research as explained by Denzin et al. (2000) include participant observation, in-depth interviews, and focus groups. For the purposes of collecting data on the perception and response of directors or boards made up of directors, in-depth interviews were deemed the most suitable.

This method is optimal in collecting data on individuals' experiences and perspectives, especially where expert knowledge is sought. However, this method requires comprehensive understanding of the critical questions to ask, the best way to ask these questions, and understanding the range of possible responses.

In-depth interviews can be structured or unstructured. Semi-structured interviews plough a path between structured and unstructured interviews (Cohen & Crabtree, 2006). Such interviews are often referred to by researchers as 'conversations with a purpose'. In a semi-structured interview setting, the interviewer and the interviewee are on an equal level. Although the interviewer knows the direction that the interview must take, he or she still allows the respondent the option to explore different paths and thoughts. According to Saunders and Lewis (2012), a semi-structured interview provides the interviewer with the ability to cover a list of questions to be asked.

The researcher used semi-structured interviews for the purpose of the study. Such a choice was made for the following reasons:

- Semi-structured interviews were well-suited to exploring opinions by probing for clarification of these inconsistencies. This methodology allowed participants to reflect their perceptions in an interview (ibid)
- The questions were fairly complicated (.)
- Semi-structured interviews allowed participants with different histories, experiences and backgrounds to reflect this in the interview.
- Semi-structured interviews allowed the use of probes (While, 1992). Probing ensures reliability of the data by asking follow-up questions when and where the answers are not fully understood.
- Semi-structured interviews allow a coerced participant to recall information from memory to be able to answer the question, providing the interviewer with richness of knowledge (Smith, 1992).

According to Cohen et al. (2006) some of the characteristics of semi-structured interviews include that the interviewer and respondents engage in a formal and proper interview, and that the interviewer uses an interview guide in the interview (to ensure that all questions are covered in the interview).

The interviews were conducted with each respondent in the privacy of their office boardroom to avoid potential distraction. The order and depth of the questions in the interviews was dependant on the experience of the participant on the particular topic.

The interviews ranged between thirty five and fifty minutes and during that time the interviewer managed to get the respondents' full attention. To ensure that the interviews were captured accurately, a recording device was used. The researcher also compiled handwritten notes during the interview while to maintain the respondents' attention. The

handwritten notes were used to augment the interview recordings and some of the salient features such as gestures and facial expressions.

4.5 Population and sampling

The following are widely used steps in selecting a sample, regardless of the specific type of sampling used:

- Identification of the target population;
- Identification of the accessible population;
- Determination of the size of the sample based on representativeness; and
- Selection of the sample.

4.5.1 The population for the research

The population that allowed the researcher to acquire an in-depth knowledge into the research comprised the following:

- Directors of listed companies; and
- Directors of previously listed companies.

It is not necessary to collect data from the entire population in order to obtain valid findings (Denzin & Lincoln, 2000). A sample of the population is sufficient to provide valid findings. The size of the sample is often determined by the objective of the study or research, as well as the characteristics of the population to be studied.

4.5.2 Sampling unit

The sample unit or unit of analysis is the board of directors of public companies in South Africa.

4.5.3 Sampling technique

A sampling framework was drawn up based on the population described above. This is based on the fact that the total population size can be determined, based on data available from the Johannesburg Stock Exchange (JSE).

A non-probability sampling approach, adapted from Saunders and Lewis (2012), was used for the following reasons:

- The research topic required subjective judgement of the researcher, based on academic literature and the experience of the researcher.
- The aim of the research was to find finer details of the sample being studied, not to make generalisations.
- Non-probability sampling was useful in exploratory research.
- The aim of the research was to end up with a sample that is proportional to the population being studied.

Non-probability sampling used by the researcher included:

- Convenience sampling, ensuring accessibility of the sampling units;
- Purposive or judgement sampling, allowing the researcher to pre-select the criteria relevant to the research question and to be able to rely on judgement when selecting the sampling units; and
- Quota sampling, allowing the researcher to determine how many people are adhering to which particular characteristics to include in the research. This is especially useful to ensure that not all participants are from a similar board, industry or shareholder group.

4.5.4 Sample size

Samples which are used for qualitative studies are generally smaller than those used in quantitative studies due to the researcher's focus on meaning rather making generalised hypothesis statements (Mason, 2010). This is also due to the diminishing returns of qualitative samples (Ritchie, Lewis & Elam, 2003). Qualitative samples must, however, be big enough to permit different views to be taken into account and to avoid sample saturation. Mason (2010) argued that sample saturation happens when the collection of new data does not shed any further light or add value to the research investigation. Guest, Bunce and Johnson (2006) opine that the smallest acceptable sample in qualitative research is about ten. Based on this, the researcher decided to obtain a sample of 15.

4.6 Interviews

The interviews were recorded using an audio recorder and transcribed into Word format. The following table gives information pertaining to each interviewee, including their position, industry and the number of years they have served on the board, as well as any noteworthy comments by the researcher.

Table 3: Interview information and characterisation

Ref	Position	Industry (Category defined as per JSE codes)	Comments	No. of years on the board	Code
1	Non-executive director	Gaming and Leisure	The respondent is also a non-executive director in a media and entertainment company	4	GND1
2	Non-executive director	Banking	The respondent is also a financial director in an investment company	7	BND1
3	Executive director	Financial Services	The respondent is the CEO of a previously listed asset management company and also sits on the board of several listed companies	7	FED1
4	Executive director	Information Technology	The respondent is also a shareholder in the business	11	ITED1
5	Non-executive director	Insurance Industry	The respondent serves on the boards of several public unlisted companies and is also a shareholder representative in the board of the insurance company	2	ISND1
6	Non-executive director	Security	The respondent has more than 15 years serving on boards of both listed and unlisted companies	3	SND1
7	Non-executive director	Banking	The respondent has more than 15 years serving on boards of both listed and unlisted companies	6	BND2
8	Non-executive director	Industrials	The respondent has served on the boards of both listed and unlisted companies – pharmaceutical, industrial and mining	2	IDND1
9	Executive director	Banking	The respondent is a highly regarded executive in the banking industry, with strong corporate finance experience	5	BED1
10	Non-executive director	Industrial	The respondent is a retired CEO of a listed company and still serves on the board of a listed insurance company	6	IDND2
11	Non-executive director	Information Technology	The respondent heads up a group secretariat of a multinational IT company.	2	ITND1

Ref	Position	Industry (Category defined as per JSE codes)	Comments	No. of years on the board	Code
12	Non-executive director	Media	The respondent is a retired chairman of both a mining and media company. He currently serves on the board of an industrial and financial services company	10	MCM1
13	Non-executive director	Mining	The respondent is employed in the investment industry and also serves on the boards of both a mining and building and construction materials company	3	MNND1
14	Non-executive director	Building and Construction Materials	The respondent also serves on the board of a listed gaming company	4	BCMND 1
15	Non-executive director	Business Support Services	The respondent serves on the board of an asset management company	9	BSSND 1

Source: Created by the researcher

4.6.1 Preparing for the interviews

Steps that the researcher undertook to prepare for the interviews included the following:

- Identification of likely participants to be interviewed;
- Development of an interview guide to assist the researcher in streamlining his or her thinking;
- Drawing up a consensus form to clearly define the rules of the interview and confidentiality clauses;
- Obtaining all the relevant information about the participants, including name, company and position;
- Contacting the respondent to explain the reason for the interview;
- Sending the consent form;
- Deciding on a suitable location for each interview, and
- Arranging for the recording of the interviews, including use of the recording device.

To ensure the best outcome from the interview process, the following aspects were taken into account:

- The researcher started the interview with the open-ended questions;
- The researcher let the respondent do a lot of the talking;
- The researcher covered all critical topics included in the interview guide; and
- The researcher ensured that her attire was appropriate for the interview to maintain a high level of professionalism.

4.6.2 Data analysis

In order to be able to answer the questions in Chapter 3, a latent level of analysis was required, which was a more interpretive analysis that does not only look at response but at what has been inferred or implied as well.

According to Miller and Crabtree (1999), the most common steps listed by researchers in analysing qualitative data include the following:

- Documentation of the data and the process of data collection;
- Organisation or categorisation of the data into different notions to provide analytical insights;
- Establishing a relationship and inter-connectedness among the different concept;
- Validation of data by assessing other possible explanations, disproving evidence, and searching for negative cases; and
- Reporting the findings.

4.7 Preparation of Data

Text qualitative data was used. Saunders and Lewis (2012) define text qualitative data as data that has been collected using audio recordings and transcribed to convert into text or Word format. No statistical or data software was used as no codes can be assigned to the individual answers.

Saunders and Lewis (2012) list the following steps in preparing data as text:

- Inclusion of date, time and place of interview;
- Use of pseudonyms for the respondents to protect their identity;
- Use of italics to indicate interview questions;
- Use dots to indicate the pause and estimated time of the pause during interviews;
- Inclusion of the researcher's description of what is occurring during the interview; and

- Use of capital letters to indicate a loud tone by the participant during the interview process.

4.7.1 Preliminary analysis of interview data

Data texting makes way for the data analysis process which Woods (2011) defined as a process of identifying, categorising and coding patterns or themes found in the data. The first step in analysing data was to read through the interview responses to look for possible patterns or themes among the data collected. The success of this process depended on the analytic abilities of the researcher.

4.8 Research limitations

The following limitations were identified when conducting the research:

- Not many companies could differentiate between shareholder activism and shareholder engagement, making it difficult to obtain data. Interpretation of the research topic is a challenge. Saunders and Lewis (2012) warned of an impact in research methodology when a researcher has to adapt to accommodate different interpretations of the topic or study by the interviewees.
- Exploratory interviews were time-consuming and may have deterred participants from taking part in the interview process.
- The use of non-probability sampling resulted in a non-representative sample.
- Interviewers did not discuss the negative aspects of their principal-agent relationship due to the fear of reprisals.
- Exploratory research was performed to gain insights into a new phenomenon and does not provide definitive conclusions (Saunders & Lewis, 2012).
- The use of an occasional spontaneous question in an exploratory interview made quantifying and analysing the answers difficult.
- The use of spontaneous questions on some respondents and not others could be seen as unfair or possibly misleading.
- The interview process required skill to avoid generalisations and possible bias.

CHAPTER 5

FINDINGS AND RESULTS

5.1 Introduction

This chapter presents and details the findings and results pertaining to the research questions presented in Chapter 3. These results and findings were based on the qualitative inquiry derived from the 15 semi-structured, in-depth interviews. The results presented herein will be further discussed in an in-depth analysis in Chapter 6, where they will be compared to the findings from the literature review.

5.2 Responses

A total of 15 directors were interviewed. All the directors selected have served on more than one board and in different industries, and not only discussed shareholder activism from the point of view of the boards they were selected for, for the purpose of the interview but also made it an encompassing discussion that brought clarity and familiarity to other industries that the research sample had not covered.

5.2.1 Respondents' information and characterisation

The respondents are from diverse background in terms of age, gender and experience. Both genders are well represented, removing any behavioural bias that impacts on the directors' responses.

The role of the directors in the various boards is relevant. Of the 15 directors interviewed, four are executive directors on the boards selected, while another four are executive directors in their daily jobs, or retired executive directors. There are slight differences and nuances in how non-executive and executive directors deal with shareholder activists.

The characterisation of the respondents has been set out in Table 4 below for ease of reference.

Table 4: Respondents' characteristics

Ref	Position	Industry (Category defined as per JSE codes)	No. of years on the board	Code
1	Non-executive director	Gaming and Leisure	4	GND1
2	Non-executive director	Banking	7	BND1
3	Executive director	Financial Services	7	FED1
4	Executive director	Information Technology	11	ITED1
5	Non-executive director	Insurance Industry	2	ISND1
6	Non-executive director	Security	3	SND1
7	Non-executive director	Banking	6	BND2
8	Non-executive director	Industrials	2	IDND1
9	Executive director	Banking	5	BED1
10	Non-executive director	Industrial	6	IDND2
11	Non-executive director	Information Technology	2	ITND1
12	Non-executive director	Media	10	MCM1
13	Non-executive director	Mining	3	MNND1
14	Non-executive director	Building and Construction Materials	4	BCMND1
15	Non-executive director	Business Support Services	9	BSSND1

Source: Created by the researcher

5.3 Understanding of shareholder activism by South African directors

The following main themes were identified from the respondents' data when invited to talk about their understanding of shareholder activism in the South African context:

- Theme 1: Shareholder activism relates to shareholders taking an active role in the company in which they have invested.
- Theme 2: Shareholder activism is when shareholders try and influence certain decisions or the direction of the company for the benefit of shareholders.

- Theme 3: Shareholder activism is really about addressing governance issues in companies.

5.3.1 Shareholder activism relates to shareholders taking an active role in the company in which they have invested.

GND1 defined shareholders activism as:

"A phenomenon whereby shareholders take an active role on the activities of the companies. This is over and above management involvement. Shareholder activists hold management to account."

This definition was supported by FED1, who stated that shareholder activism is:

"Shareholders who take a much more active role in the decision making of the company in terms of strategy, remuneration and so on. Voting in shareholder meetings not in terms of proxy but by attendance."

5.3.2 Shareholder activism is when shareholders try and influence certain decisions or the direction of the company for the benefit of shareholders.

The second theme that emerged from the interviews is that shareholder activism has to do with shareholders seeking to influence the company by improving returns and performance. By influencing the companies, they are also seeking to protect value.

IND1 identified shareholder activism as:

"People who want to influence the business in favour of shareholders who are not represented on the board by seeking to guide strategy or business direction."

5.3.3 Shareholder activism is about addressing governance issues in companies

The third theme that emerged is that shareholder activism is in response to the heightened need for governance in South Africa to the latest version of the companies' shareholders and King Code of Governance. The respondents relate shareholder activism as a process that is undertaken to address issues not appropriately dealt with or covered by the board of directors.

BCMND1 summarised the theme by defining shareholder activism as:

"Shareholder activism is really about issues of governance in a company. The overall objective of shareholder activism is to improve governance in companies and transparency and accountability of the board members. In most instances it comes through when individuals or the shareholder activists whether as individuals or representing companies or funds, when there's some level of unhappiness with how the board is conducting itself and in general around governance issues, whether one looks at it at a company level or country level."

From the viewpoint of South Africa, the first thing that comes to mind is that shareholder activism is seen as a confrontation between the shareholders and management because that is what seems to receive media coverage.

5.4 Shareholder activists in South Africa

One interesting theme that emerged from the data is how different directors or companies view Theo Botha, a self-proclaimed. South African shareholder activist. The respondents classify shareholder activists into two categories: Theo Botha and the more serious institutional shareholder activists.

INDN2 put this into perspective:

"Shareholder activism over the last couple of years was an activity where one or two individuals (like Theo Botha) will come to a company to question their governance and some of their remuneration policies and really try to act like the shareholder or the representative."

This was collaborated by MNND1:

"The individual shareholder activist that I have dealt with is Theo Botha. The more serious activists we have seen are the likes of [the] PIC (Public Investment Corporation) and the asset managers. Asset managers are becoming more of shareholder activists."

The institutional shareholder activists according to most respondents typically include pension funds, insurance companies and asset managers that have significant shareholding and seek to influence the company by improving returns and performance.

Some respondents associate shareholder activism with minority shareholders due to the fact that they do enjoy the same privileges as the large shareholders and therefore the activism route as the only conduit for them to be heard.

Another grouping that emerged from the data was hedge funds. MCM1, chairman, of a previously listed company noted that he experienced this type of shareholder activism. He said:

"This shareholder became very active with an intention of a hostile takeover. This was a grouping called Active Value, which were guys from the UK who gradually bought a very substantial number of shares in the company with an intention of staging a hostile takeover."

The other strategy that hedge funds use is to buy a share on a back of a short-term strategy in undervalued companies. They get actively involved with the companies to unlock value which they believe is trapped in the businesses.

Some respondents mentioned environmentalists who have an environmental agenda. In complying with governance frameworks, companies are also focusing on the broader stakeholders than necessarily people who hold shares and therefore shareholders, these stakeholders can be the shareholders themselves, the community, customers or even staff members.

5.5 The impact of shareholder activism on South African companies

Another theme that emerged is that the impact of shareholder activism on companies can be both positive and negative. The positive aspect tends to enhance value, while the negative aspect tends to be a disruption to management's mandate of running the businesses. ITED1 summed it up nicely:

"I think whether they [are] disruptive or not depends on the relationship between the shareholders, management and the board. They also depend on how management and the board deal with them and the issues that they raise."

The overall theme is that the impact of shareholder activism is more positive than negative. This can be seen in a comment made by MCM1:

"Typically what you will find is that everyone knows about the disruptive side and not a lot of people are talking about the supportive side."

5.5.1 Positive Impact

The theme from the data indicates that in principle, shareholder activism enhances governance structures. Shareholder activists can protect value by upholding governance principles, thereby protecting the reputation and long-term value of the company. The respondents seemed to agree that shareholder activism impacts positively on how companies run in the long term. This was evidenced by ITED2, who summed up the root of shareholder activism in the context of South Africa:

"If I look at SA in the 70s and 80s, there were small groups of activists in the corporate spaces who agitated multinational companies to withdraw their investments in SA during the discriminatory laws that existed at that time. So that obviously had a positive effect and future for South African corporate space. That is one way of looking at it from a positive point of view."

There was also a perception among respondents that shareholder activism has brought to the fore certain issues which may not have been given adequate audience or attention in the past, such as tenure, independence and remuneration of directors. In most instances, shareholder activists improve performance by holding management to account.

Another theme that emerged from the data in terms of the positive aspects of shareholder activism was that shareholder activism improves disclosure, thereby increasing transparency. In the same line of thinking, BED1 also identified transparency as being the key positive aspect to shareholder activism:

"I think I am for more transparency, so the more the better. Largely, corporate governance framework is quite rich in detail, in terms of requiring companies to disclose specifics like remuneration of executive directors and prescribed officers and in the main, what shareholder activist do is to insist on more disclosure, where they think there isn't enough disclosure by asking more questions. Those have come largely in particular areas."

5.5.2 Negative impact

The first theme that emerged from the data is that, although shareholder activism is in the main, positive, it can also be disruptive. This was the view of BED1, who is the executive director of a bank and who is on the cold face of shareholder activism from

shareholders and stakeholders, such as the regulators and the environmentalists. He said:

"First of all, activism as a term, has a negative connotation and particularly because these shareholders tend to participate when in their view things are not going well or they are addressing issues they don't particularly support in that company. From that perspective the manner in which they choose to address these issues can indeed be disruptive."

The second theme that emerged was that shareholder activism can be disruptive if it goes against how the company operates. These real disruptions to management come when the battle between management and the activists takes its toll on management and distracts them from daily running of the business. These battles are often played out in public and create uncertainty around the future of the company.

Another common theme was that shareholder activists often take decisions that are not informed by what the company or management is doing. Shareholder activism varies from one shareholder to the other but has to do with the depth of understanding of the business to which they are focusing on at that moment. The perception from the data analysis was that they take an adversarial or confrontational stance by pointing out what the company is not doing without really engaging with the board first.

Lastly, strongly embedded in the data was the notion that shareholder activism ultimately seizes a substantial amount of control from the board, causing boards to consult shareholders for every important decision that needs to be made. This often resulted in the slowing down of decision making in the company.

5.6 Key drivers of shareholder activism in South Africa

In analysing the responses for key drivers of shareholder activism in South Africa, the following key themes emerged from the data:

- Performance;
- Changes in legislation;
- Transparency and disclosure of information equally to all shareholders;
- Uses of cash in the business; and
- Governance-related issues.

5.6.1 Performance

One of the key drivers of shareholder activism is performance to enhance shareholder value. Shareholder activists often voice their views where performance of the company is seen to be deteriorating. The deterioration can be against budgets or forecast, prior periods and industry players or indices. This view is supported by FED1, who said:

"Shareholder activism is often more prevalent in companies and management teams that are under-performing especially in relation to their peers and their sectors."

5.6.2 Uses of cash in the business

The concept of a "lazy balance sheet" came up frequently in the data as a key driver of shareholder activism. The respondents associated this concept with a need for cash by the shareholders. The perception is that the "lazy balance sheet" is often one of those agendas that a shareholder puts on the table and which is driven by the shareholder's own selfish interest. This was supported by BND2, who said:

"We have cases when the shareholder looks at our balance sheet with the aim of stripping out cash. When the term 'lazy balance sheet' is bandied around, you know it is time to look at special dividends and or share buybacks – with share buyback, their shareholding remain the same but at the same time they cashed in on this huge dividends."

BSSND1 concurred with the view:

"They are various strategies that shareholder activists deploy to access excess cash, such as changing the dividend policy, share buyback and so on."

5.6.3 Transparency and disclosure of information equally to all shareholders

Non-disclosure for minority shareholders is the single-most driver of shareholder activism. The general perception is that minority shareholders do not have the same access to the companies' information as the large institutional shareholders and are often left out of big decisions or only get the information after the fact. This has increased the need for activism on the part of minority shareholders. The plight of the minority shareholders was highlighted by SND1:

“It is mostly minority shareholders that do not necessarily get full disclosure about certain key issues in the company. When companies embark on road shows or information sessions their plans do not normally include minority shareholders, maybe because it is a logistical nightmare to consider all shareholders, but they don’t. These shareholders are left with no other choice but to use the remaining avenues left for them which in this instance is shareholder activism.”

IDND2 also supported the view that the non-disclosure was selective and used as an exclusion tool. He said:

“I think, historically, one of the drivers of shareholder activism was a consequence of exploitation and of insider trading and people got fed-up with that and a lot of non-disclosure of information.”

Another information requirement is linked to the remuneration of executives and the remuneration policy. There are a few reasons for the increased hype around remuneration policies as evidenced in the data. One of the reasons was outlined by IDND2, who said:

"I think what some shareholders are asking for is transparency in terms of remuneration of key officers. They are looking to see if there is a balance between the performance of the company and the remuneration of the executives."

5.6.4 Changes in legislation

The theme that emerged is that, following the implementation of the new Companies Act, shareholders started exercising their legal rights in pursuit of their activist agenda. These rights became applicable to all public companies, and others to just listed companies. This view was supported by BSSND1, who said:

"The first driver I can think of is the Companies Act, not so new but reasonable new. If you look at the some of the new provisions of the act, such as the enhanced rights of the minority shareholders for example, this created an environment that supported shareholder activism. A lot of these activists are very much aware of these legislative changes and all the rights that come with them."

The other piece of legislation supported by the data that is driving shareholder activism according to the respondents is the King III report. BND1 summarised below the link between increased activism and King III:

"According to King III, shareholders should approve the company's remuneration policy. This has put shareholders in a precarious position. For them to approve the policy, they need to satisfy themselves that the remuneration is fair and responsible. This has increased the executive remuneration based shareholder activism."

King III also emphasised enhancing the responsibility of boards of directors, making shareholders the "ultimate compliance officer" (as MNND1 put it). According to MNND1, shareholders now need to have the responsibility to appoint an audit committee.

5.7 Common demands made by shareholder activists

The following themes were identified from the respondents' data when asked about the common demands made by shareholder activists: executive remuneration, request for information, control of unissued share capital, and directors' governance matters.

5.7.1 Executive remuneration

Interestingly, some 90% of respondents had these as a common demand made by shareholder activists. This seems quite topical in South Africa at the moment, as indicated by IDND2, a seasoned non-executive director, who said:

"One of the most debated and dominant issue has been the remuneration of the executives."

The trend for shareholder activists is to raise the issue of executive remuneration, especially executive bonuses and pay raises, and compare this to the performance of the company. This is to ensure that management remuneration is in line with shareholder returns.

5.7.2 Request for information

The results from the data indicated that shareholder demands are mostly in terms of the information surrounding adherence to regulations. GND1, a non-executive in a gaming industry, confirmed this assertion by saying:

"Most of the demands are also around access to information to ensure compliance."

Analysis of the respondents' data also revealed that shareholder activists often ask the directors to provide information or clarification that they deem necessary about certain items on the agenda of the AGM, or pose questions they deem appropriate, to which directors are obliged to respond. The shareholder activists want to ensure that the reputation of the company that they have invested in remains intact.

5.7.3 Control of authorised unissued share capital

The control of authorised unallocated share capital is strongly grounded in data as a common demand made by shareholders. According to the respondents, the control of unallocated unauthorised share capital has always been left in the hands of directors until the next AGM, and this item was always a non-issue in the AGM. It was a 'tick box exercise'. Of late, shareholders have been questioning the control by management. This sentiment was illustrated by ITED1, an executive director in a financial services company, who said:

"Some of the common demands made by shareholder activists are around giving management full control of authorised unissued shares – the general feeling is that it should not be prerogative of management to issue these shares."

5.7.4 Directors and governance

A theme that emerged from the data indicated that shareholders as the custodians of good corporate governance have started to put pressure on the boards regarding the affairs of directors. One of the demands in this regard, according to the respondents, is the removal of directors from office. According to SND1, shareholders now have the power to challenge directors for their board seats. This was supported by IND1, who said:

"It is not uncommon for shareholders to remove the whole board or some members of the board if they feel that the board is ineffective in fulfilling its mandate."

The respondents brought up, several times in fact, the question of the independence of the board. Shareholders activists have also questioned the tenure of some directors and linked the length of service to their independence or perceived lack thereof. A common dilemma that boards face in terms of tenure and independence was summed up by ITED2, a group secretariat in an IT industry, who said:

"The issue of long service of directors and their independence has also come up often. It is an important point, but it is hard to explain it because you need to balance it as a company. Yes, you want good minds and you want the right people to direct the company, but at the same time you also want to make sure that it is as independent as can be."

Another common theme under this sub-heading is the attendance record of board members. It was supported by BED1, who said:

"Another issue that is common is the attendance record of board members. Shareholder activists normally take an exception to that and often choose not to vote in favour of that director to continue to be on the board."

5.8 Strategies commonly employed by shareholder activists to realise their demands

One interesting sub-theme that emerged in analysing the type of strategy used is dependent on the size of the shareholding in the particular company, which may range from passive to aggressive. The following demands were strongly supported by data as common strategies employed by shareholder activists in realising their demands.

5.8.1 Direct communication with management or the board

This was regarded by many respondents as by far the more passive strategy used by shareholder activists. This strategy, according to the results, is often used by majority shareholders as they have relationships with the company and with management. Accordingly, this platform is also used to update the activists about the various issues relating to the business. This strategy was confirmed by GND1, who said:

"The South African market is a prominent category but it is quite limited. Your large institutions and established institutions tend to deal with issues behind the scenes. The South African market tends to want to settle things across the table or behind the scenes as opposed to in the public."

This perspective was also supported by BND2, who said:

"Large shareholders, because of the size of their stakes, tread very carefully and are not aggressive in dealing with the board."

Direct communication was regarded by the respondents as the most effective way to engage the company by many respondents. This perspective was supported by BED1, who said:

"The most effective way for activists to engage the company is through the company's investor relations. Investor relations engage with shareholders throughout the year, so shareholders are able to ask for meetings with whomever they seek to meet. It could be the chairman of the board, CEO, CFO, or someone in management, to provide explanations or clarification on pertinent issues."

5.8.2 Lobbying of other shareholders

According to the respondents, one of the most common strategies used by shareholder activists to realise their demands is through lobbying of other shareholders. This strategy as evidenced in the respondents' data is used by both large and minority shareholders. Large institutional shareholders use this strategy to lobby other large shareholders while the smaller or minority shareholders use the strategy to lobby the larger shareholders, as explained by IDND2, who said:

"These large shareholders sometimes don't attend AGMs and vote by proxies instead. The small shareholders normally take advantage of that fact – they are aware that there are floating votes from these shareholders and what they would do is to approach them with the issues they would like support on and request the use of their proxies to effect that. If the smaller shareholders are on top of their game and have done their homework properly they are normally able to get support of these large shareholders. The success of their strategy is very much dependent on the whether or not they are able to convince these large shareholders."

Large institutional shareholders also do their own lobbying behind the scenes with management, explained by GND1, who said:

"In some instances, if an institutional shareholder is large enough, like the PIC or Old Mutual, there may be an engagement prior to the AGM in which the intention of that shareholder's vote will be made known to management and the board in the hope of trying to steer a different outcome."

5.8.3 Attendance of the AGM

A three-pronged strategy has been identified from the respondents' data in terms of the use of AGMs by shareholder activists to realise their demands. The first strategy as identified by respondents is to openly challenge or raise issues in the AGM to the board or management, while the second is to raise issues before the AGM and request management to address these issues in the AGMs. The third is through voting and shareholder resolutions, where they either vote down certain resolutions or vote in favour of those resolutions.

The methodology used once again depends on the relationship between the shareholder activists and management, the size of the shareholding and the type of issues. This perspective was supported by IDND2, a very experienced non-executive director on numerous boards, who said:

"This depends on shareholders. Some take a gentle approach by writing to a Chairman of the board, or CEO and list their concerns. They could put a request for the board to address the issues that they have in the next general meeting or request for plans to be put in place to address their concerns. The other strategy used is to utilise an open Q&A session in the AGM to raise issues they are concerned about. The latter is common in protest type queries where they strongly challenge issues or when they want to embarrass the management and the board on certain types of issues."

5.8.4 Use of public media platforms

The trend in the use of public media platforms by minority shareholders to effectively get their message across is strongly grounded in the data accompanied by various examples:

"Minority shareholders go public. I suppose they would engage companies, management or the board but in my experience they find going public with their issues is what raises attention. As these are normally minority shareholders, they may not be able to sway the direction of the votes, for them to influence other shareholders and to make sure their votes are heard they do that through the media."

The trend observed by several respondents is for some shareholder activists to bring media to the AGM to increase create a huge hype around issues or demands:

"They talk to the press and you might find that some of the activists even brief the press before the meetings and inform them of their intentions to raise some contentious issues that they are going to be fuel for the fire."

Media platforms can also be used by the board to create awareness and understanding of certain issues in the company before they get blown out of proportion. This was evidenced by BSSND1, who said:

"I would like to give you an example without quoting the company that I was involved in once. The company is a large public company and they were having some difficulties. I remember arranging for a meeting with a journalist who was quite a busy person and activists prior to the AGM of the company. I told them what was happening in the company and told him why we were going to be doing the things we were planning on doing. I was happy to handle any questions that they had. There was a very welcome response from them. I really believe that a lot of the responsibility belongs with the company and the management. All companies will go through a difficult period from time to time. And if they do get these activists, it is the responsibility of the companies to explain to them what is happening in a transparent manner."

5.9 Issues that have been elevated to South African board agenda as a result of shareholder activists demands in the last three to five years

Key themes that emerged from the respondents' data on issues which have been elevated to South African board agendas include the following:

- Executive remuneration or remuneration policies
- Directors' independence

- Transformation
- Companies' levels of indebtedness.

5.9.1 Executive remuneration or remuneration policy

The trend is very strongly grounded in the data. An overwhelming number of respondents stated executive remuneration and or remuneration policy as the most common issue that was elevated to the board agenda as a result shareholder activism. The boards have been put under a lot of pressure to review the executive remuneration in line with the company's performance and to disclose as much information as possible, the quantum of these payment and how these amounts were derived at. This was supported by BED1, who said:

"The first one is the remuneration policy. Although it is commonly accepted that integrated reporting is the summarised version of the old sustainability report of the annual financial report, one thing that is not summarised in the report is the remuneration policy, it has to be disclosed in full. The company has to state how the remuneration policy was applied in relation to what has happened during the reporting year, as well as publishing remuneration of prescribed officers."

Another issue that came up and but was not strongly grounded by data is fees paid to non-executive directors.

5.9.2 Directors' independence

The issue of long service of directors and their independence also came up often in the respondents' data.

5.9.3 Transformation and BEE

Transformation was another theme that emerged from the data. In fact, it so happens to be the issue with which the board of the security company is currently dealing. This has been elevated to the board and has become an agenda item at board meetings because the company is failing to meet its transformation and BEE targets which, in South Africa, has become something of a business imperative.

5.10 The response of South African boards to shareholder activists' demands

The main theme identified from the respondents' data when asked how the boards that they are sitting on or sat on responded to shareholder activists' demands was that of compliance and cooperation. There is very little evidence from the results of an adversarial relationship between the board and shareholder activists. This perspective was supported by BSSND1, who said:

"We have not had an unreasonable demand from shareholders activists in the past. In most instances we received a request from them and worked around the table to try and meet the demands. We take our activists demands seriously and take into account that they often bring skills to the table that the board may not possess."

SND1 added that the following:

"A committee made [up] of the sub-board members and management was set up. This was specifically to address the transformation issue raised by the shareholder activists. The board set the targets that management had to meet and there has to be a valid explanation as to why the targets are not met."

5.11 The role of the board in dealing with shareholder activists.

The first theme identified from the respondents' data when asked what they think the role of the board should be in dealing with shareholder activists was to be accommodative as much as possible to their demands but still be able to act in the best interests of the company and all other shareholders. This theme revolves around objectively considering the activists' ideas or demands. This view was supported by BCMND1, who said:

"The role of the board in dealing with shareholder activism is to reflect on the demands made by shareholder activists and decide on the best way forward. The ultimate decision should be for the best interest of the company and for all shareholders. The board has many decisions to make and in that process should incorporate the demands made by the shareholder activists."

It is the respondents' perspective that the responsibility of the board is to manage the relationship between the shareholder activists and the company to ensure that it does not become adversarial. This was supported by a view of BND2, who said:

"You have to manage them. As a board you want to know how management deal with the issue and want to assess as well that they are not dismissive, and make sure they have a response to the issues at hand or a plan on how to deal with the issues raised as well as a team which is focused in dealing with these issues. So you want to make sure they are receptive to providing a response because the relationship can get very adversarial very quickly. For example at the (...) board when a shareholder activist raised a contentious issue, we had the big institutional shareholder like (...) and (...), some members of the board, as well as management dealing with the issues raised by the shareholder activists."

The perspective of the respondents in cases where the boards hold different views from that of the shareholder activists is to evaluate the shareholder demand in line with the board mandate and act accordingly.

"I think it's important for the board to address them if they are raised in a responsible manner; it's not for the board to just shut them out. Also there is no substance or maybe that there are not material they need to feedback to the activists in a rational manner."

The second main theme that came through in the respondents' data, though not as prominently as the first, was that the role of the board is to keep the shareholder activists well informed and be as transparent as possible. This view was supported by IDND2, who said:

"The role of the board in dealing with shareholder activists is to keep them well informed. Prepare for shareholder engagement in advance. I really believe that that is a very fundamental thing to do. I mentioned earlier that remuneration today is very topical area and very contentious. I think if you have substantial shareholders then you should be prepared to share your remuneration policy and your incentive scheme, your LTIPs and all that stuff with them to get them to get their buy in as to why you are doing it, the need to understand your motivation for these particular things so that they can become part of the process. Management have a big role to fill at the AGM, they should be prepared to be fully transparent on these issues. I don't have any difficulty, depending on the size of the company, having shareholders visit the company to understand the business of the company. All these things help people to find synergy in the relationships."

The last theme under this heading which was prominent from the interviews but not as strongly grounded in the data as the other two themes is the overall statutory responsibility of the board regardless of whether they are dealing with shareholder activists or not. This perspective was supported by BED1, who said:

"The board should always remember that the ultimate responsibility for the affairs of the business and the sustainability of the company lies with them and that is in terms of the legislation (Companies Act, 2008) and King Code of Corporate Governance. The role of the board is to oversee that the company is taking responsibility of the interests of all its stakeholders. Its key primary role is to make sure the affairs of the company are running correctly."

This was reiterated by BCMND1, who said:

"The starting point is you have to act in the interest of the company. Which by implication you act in the interest of all shareholders as opposed to those particular shareholders raising an issue. You cannot therefore act on a basis of single shareholder who is demanding the certain outcome acting that outcome unless if that is deemed to be the interest of the company as a whole. So that is quite fundamental to how a board must act and this is irrespective of members of the board may have been nominated by shareholders to be on the board. The board needs to act for all the shareholders. At the same time though you do need to listen to what the concerns are."

The role of boards in looking after the best interests of the company should be balanced. This view was supported by MCM1, who said:

"I think that boards should play a balancing act. The board should function in the best interest of the company while ensuring that the value that the shareholders have put into the company is not reduced or diminished."

5.12 Preparation for shareholder activists' engagements

What emerged from the data under the heading of preparation for shareholder engagements is that nearly all respondents prepare for shareholder activists' engagement but do so to varying degrees. The data revealed that some companies prepare extensively for shareholder activism, as described by BED1, who said:

"Our board has taken a view that first of all the company should have a very proactive and well qualified investor relations, and through that process we spend a lot of time talking to the shareholders formally. During the results periods we will spend at least a week with the local shareholders and another week will be the international shareholders, so we hold approximately 280 meetings per year of just seating with the shareholders and our coverage is to reach 85% of all the shareholders and obviously most of the shares are represented by institutions so we will seat down with them and go through the results and the key drivers for the performance of the business.

Secondly, the our board recognises that through investor relations generally the shareholders are engaging with the management so once a year we have a governance road show where the chairman accompanied by the independent lead director will go through a similar process of a road show with the shareholders and they then talk to shareholders themselves without executive management so that if shareholders have any concern regarding governance or other things that they don't feel comfortable to address with management or they feel they have addressed with management and still not resolved.

Thirdly, the board requires an independent feedback which is often conducted through a broker like (...) and those institutions will contact people or institutions who are already shareholders in (...) or potential shareholders and just ask them questions around strategy of (...), the performance of the business, their perception about management, their perception about (...) in relations to other banks as well as the perception about the banking sector so then the board gets that report unfiltered by management and that gives them a very independent view about how shareholders or potential shareholders perceive management and that they match that with their own understanding of the stats of how the company is performing.

In the preparation, it's also important to know who your shareholders are. The 85% coverage gives a view of who the shareholders are. You understand the nature of that shareholder so when you engage with them you know the kind of things that are important to them."

Some companies prepare moderately, as in the case of the IT company, evident through what ITND1 said:

"Engage on a regular basis, at least three times a year. The company ensures that they have interaction with major shareholders at least once in a 12-month period. This interaction happens with the chairman of the board, executive management, the chairman of the audit committee and discussions around the direction of the shareholders."

Contrarily to this, other companies do very little in terms of preparation:

"Management presents to the board what they would be presenting to the stakeholders and it's also important for management at this point to raise any prior issues that had been raised by shareholder activists for the board to decide on how to best address those at the next engagement session."

5.13 Summary of findings and results

The interview data supports the prevalence of shareholder activism in South Africa. All industries in the country deal with some level of shareholder activism in varying degrees. The respondents in South Africa do not see shareholder activists as corporate raiders as is the case in many countries but rather, as legitimate investors seeking increases in shareholder value.

In general, it could be observed that shareholder activists have been associated with minority shareholders that call to question management activity, managers' remuneration, how managers go about managing the company and whether they are managing it with the intention of creating shareholder value. The large shareholders are not necessarily regarded by the respondent, as activists but rather as value investors.

A strong theme from the data in terms of impact of shareholder activism is that shareholder activists enhance governance and in so doing may disrupt management in their daily running of the businesses. There is a strong emphasis that shareholder activism does not destroy value.

Regarding the drivers of shareholder activism in South Africa, it could be observed that the changes in legislation have been a main driver, if not the primary driver. All the other themes under this sub-heading, such as the need for more disclosure and the governance surrounding directors, have been enabled or initiated by the legislative framework.

In terms of the demands made by shareholder activists, a one-sided approach can be observed which conceptually puts shareholder activists and management at opposing ends. The common demands made by shareholder activists according to the respondents' data are more in terms of governance and the lack and adherence thereof, and less in terms of value-enhancing strategies.

With regards to the strategies employed by shareholder activists to realise their demands, the evidence shows that South African firms prefer “behind the scenes and across the table” methods that are non-confrontational. The main reason for this is that a significant amount of shareholding in the JSE is in the hands of the same large institutional shareholders who have common shareholding in many of these listed entities.

Regarding the role of the board in terms of dealing with shareholder activists and/or their demands, local boards demonstrated that a balancing act is required. The role of the boards evidenced from the data is to consider the demands made by shareholder activists and decide on the best way forward, though the ultimate decision should be in the best interest of the company and for all shareholders.

With regards to preparing for shareholder activists in demand, the evidence shows that companies in South Africa prepare for shareholder engagements in advance, though the level and detail of preparation varies from industry to industry and from company to company. Some sectors have a detailed plan on shareholder engagements while others work on an ad hoc basis.

In an overarching view, there was a generalised perception that shareholder activism has moved up a notch in the last ten years and has improved governance by increasing transparency in the companies.

CHAPTER 6

DISCUSSION OF RESULTS

6.1 Introduction

The purpose of the study and the research presented herein is to provide a better understanding of shareholder activism in South Africa by examining it from the perspective of company directors. The study sought to explore the topic of shareholder activism by obtaining the directors' perspective on the topic, their reactions and the actions available to them in terms of how to deal with shareholder activism.

This chapter provides a comprehensive analysis of the findings and results presented in Chapter 5 in light of the comprehensive literature review presented in Chapter 2, while seeking to refine the research propositions and answer the research questions posed in Chapter 3.

The structure of this chapter follows the sequence of the research questions as set out in Chapter 3, which are cited below for ease of reference:

Research question 1: What is shareholder activism in the context of South African firms?

Research question 2: Who are the shareholder activists in South Africa?

Research question 3: What has been the impact of shareholder activism on South African companies?

Research question 4: What are the key drivers of shareholder activism in South Africa?

Research question 5: What are the common demands made by shareholder activists in South Africa?

Research question 6: What are some common strategies used by activists to realise their demands?

Research question 7: How do South African boards respond to shareholder activism?

Research question 8: What is the role of corporate boards in dealing with shareholder activists?

Research question 9: How do corporate boards prepare for shareholder activism?

6.2 Research Question 1

What is shareholder activism in the context of South African firms?

With regards to research question 1, three main definitions were provided by the respondents, as follows:

- Shareholder activism is when shareholders take an active role in the company in which they have invested.
- Shareholder activism is when shareholders try and influence certain decisions or the direction of the company for the benefit of shareholders.
- Shareholder activism is about addressing governance issues in companies in which the shareholders have invested.

The interviews conveyed that in South Africa, the type of shareholder prevalent is corporate governance activism, focusing on the firm's governance reforms. Rose et al. (2013), identified two primary types of financial shareholder activism, namely performance-driven activism (advocating for an increase) in own wealth; and corporate governance activism, focusing on the firm's governance reforms. The former is not firmly grounded in the data. The shareholder activists' action in South Africa tends to protect what they perceive as value and does not necessarily create value.

The view supports Daily and Canella's (2003) notion that shareholder activism is a very instructive tool in terms of corporate governance. In South Africa, the governance transformations pursued by shareholder activists seek to shed some light onto valid and effective governance practices of protecting shareholder interests.

In summary: research question 1

The perspectives of directors, as indicated by the results of the in-depth interviews, supported the definition of shareholder activism in the literature review in Chapter 2. There is a strong sense that the South African context seems to emphasise the corporate governance element of the definition more than the other elements. Influence and active role were the other strong constituents of the definition. Increasingly, companies in South Africa are being approached by shareholder activists who seek to exercise power and influence over their business activities.

6.3 Research Question 2

Who are the shareholder activists in South Africa?

The main activist type identified by the respondents is long-term institutional investors. Typical long-term institutional investors are large pension funds, insurers and asset managers. These shareholders typically invest for the long haul and tend to be vocal when they believe that the companies' or directors' actions threaten to destroy the value of the company.

According to Harvard Law School Forum on Corporate Governance and Financial Regulation (2012), these type of activists can be broadly categorised into 'vote no' shareholder campaigns for board best practice and for company specific. The vote no campaigns are normally a defensive activism tool used by public pension funds (Ertimur et al, 2011).

There has been little evidence of hedge funds in South Africa. Hedge-fund activity was evidenced in companies with significant international shareholding such as banks and insurance companies. Proponents of hedge-fund activism contest that it improves stock price and operational performance of the companies in which they are involved in the short-term, while critics argue that it reduces shareholders' wealth and may also result in the downgrading of certain stocks by increasing share price volatility, as well as its debt structure (Agrawal, 2012).

The success of hedge funds in South Africa has been reduced by different strategies employed by local companies to specifically deal with them. One of the strategies evidenced in the data and collaborated by respondent BED1 is to indirectly control the size of the shareholding of hedge funds. This is done by encouraging and enticing other value shareholders to take up available shares, thereby limiting the number of shares available for hedge funds. This carefully orchestrated strategy has its limitations – the more illiquid the share, the poorer it is in terms of performance.

The remaining type of primary shareholder activism as evidenced in the study is the 'say on pay' campaign type of activism, which is used by minority shareholders in South Africa to voice their dissatisfaction of the level of executive pay and to control executive remuneration. This view supports the finding that say on pay campaigns are becoming the most widely used tool to control executive pay (Ertimur et al, 2011). Ferri (2013) further argued that say on pay activism is a tool used as a threat to force management

and the board to critically review their remuneration policies, and to link these policies to performance.

In summary: research question 2

The interview findings as they relate to the type of shareholders in South Africa were consistent with the findings evidenced from the literature review in Chapter 2. All the types mentioned in the literature review, with the exception of shareholder proposals, were mentioned by the respondents. However, the changes normally advocated by these shareholder proposals, and which are sponsored by a wide range of shareholders, are normally advocated by large institutional shareholders in South Africa.

6.4 Research Question 3

What has been the impact of shareholder activism on South African companies?

According to the respondents, shareholder activism can be both positive and negative. The findings are contradictory and in line with the literature review in Chapter 2. Bizjak and Marquette (1998) and Opler and Sobokin (1997) submitted empirical evidence which proves that shareholder activism tends to improve the operations of the target companies, though Karpoff et al. (1996) argue that there is very little evidence that this is the case. Gillian and Starks (2000) reached similar conclusions.

6.4.1 Positive impact

The findings in Chapter 5 with regard to the positive aspects of shareholder activism are as follows:

- Protection of value by upholding and enhancing governance principles, thereby protecting the reputation and long-term value of the company;
- Improvement of disclosure, thereby increasing transparency in companies; and
- Improvement of performance by holding management to account.

Shareholder activism addresses unacceptable governance. Activist shareholders have created a system where they serve as watchdogs over boards and management to address governance matters. This view is supported by Smith (1996), who said shareholder activism is successful in changing governance structures which in turn increase shareholder wealth.

The evidence discussed earlier on indicated that the predominant type of shareholder activism in South Africa is institutional shareholder type activism. These activists protect value by voicing their opinions about certain elements of governance, especially in cases where they perceive certain elements of governance as being flaunted, resulting in damage to the company's reputation of long-term value. This view supports Gillian and Starks' (2007) argument that large institutional shareholders focus primarily on governance-based activism, which seeks to improve or enhance governance structures and increase management and board accountability to the shareholders.

The evidence also shows that although there are no systematic governance issues in the country, what shareholder activism has done is that corporate board and management in South Africa are always looking over their shoulders to ensure that they are not being targeted for governance shortfall in their companies. Shareholder activism has even shaped board agendas to ensure compliance.

The theme of improved disclosure as a result of shareholder activism has come up very strongly in the South African environment. The definition of corporate governance has a strong transparency theme and therefore the improved transparency comes on the back of the 'governance alert' environment. The results indicate that shareholder activism in South Africa has increased transparency especially for minority or individual shareholders that do not have access to management.

Companies have an obligation in terms of the Companies Act, the King Code of Good Governance and JSE regulations to disclose certain information. However, they have found themselves disclosing more than the recommended information to shareholders as a proactive measure to keep them at bay.

Another benefit of shareholder activism revealed by the study is that shareholder activists encourage the board and management to improve the companies' operational performance. Shareholder activists often criticise operational inefficiencies and unprofitable businesses and can recommend strategic initiatives to improve underperforming businesses (Gantchev, 2013). Shareholder activists, as indicated by respondent BND2, are normally vocal when they think the company is underperforming or not performing at the same levels as its industry or sector peers. Even if the involvement of shareholders does not get the company to improve performance immediately, management and the board become more focused and start putting plans in place to improve company performance.

6.4.2 Negative impact

A competing view is that shareholder activists sometimes pursue their own goals, which often leads them to seek a quick gain at the expense of the long-term health of the company. There is evidence in South Africa that the institutional investor, the PIC sometimes seeks to steer strategy or firm policy in a particular direction in order to pursue a political or social objectives agenda, policies such as transformation and foreign investments. Romano (1993) argued that public pension funds have a tendency to seek to alter the investment policies of the companies they have invested in to meet their political and/or social objectives. This presents an agency problem between the shareholders and the firm.

Another view that came in strongly is the view that shareholder activists tend to interfere with the daily running of the companies and, in most instances, do not have the skills or the experience to effectively do that. There are examples where they have acted on impulse without having sufficient depth and knowledge of the issues they were pursuing.

In summary: research question 3

Evidence from the respondents supported by the literature review has highlighted that having an activist shareholder can be productive, neutral or unproductive for the company; it all depends on the alignment of goals between the company represented by the board and the shareholder activists.

Another factor that came up was the ability of shareholder activists to analyse the company and its prospects instead of just simply seeking changes that would result in a short-term value increase at the expense of long-term business values.

Lastly, the perception of productivity versus non-productivity is often subject to interpretation and is dependent on who is on the other side of the line.

6.5 Research Question 4

What are the key drivers of shareholder activism in South Africa?

In analysing the responds for key drivers of shareholder activism in South Africa, five key themes emerged from the data, namely performance, changing legislative framework, inadequate disclosure, use of excess cash in the balance sheet, and governance-related issues.

6.5.1 Performance

Shareholder activism is driven by returns, and returns are driven by performance. In the main, shareholder activism increases when the company is not performing against set plans. The shareholders and shareholder activists get involved as they believe there are corrective actions which can be put in place to remedy the situation at hand.

Performance is sometimes related to the operational strategy of the company. Shareholder activists often question the strategy of a company if they perceive their value to be under threat.

6.5.2 Use of excess cash in the business

One of the key themes that emerged from the data is that South African public companies are sitting with a lot of cash in their balance sheets, the economic growth is very low and investors are looking at other opportunities to grow their money so they become restless. Most of them look to shareholder activism in order to gain access to the cash sitting in the businesses.

6.5.3 Non-disclosure of key information

Non-disclosure for minority shareholders is a key driver of shareholder activism. The issue of unequal treatment and access to information for some shareholders, especially minority shareholders, came up several times in the data. On the subject of non-disclosure of key information is the remuneration of executive directors. This is a big topic, particularly over the last three or four years, and shareholders are looking at that in relation to company performance. In essence, the displeasure of some shareholders drives shareholder activism.

6.5.4 Changes in the legislative framework

A theme that emerged is that rights and position of the shareholders, especially the minority shareholder, is supported by provision of the new Companies' Act, 2008, which has empowered shareholders in terms of their rights. These changes have supported a trend where people buying one or few shares in particular companies so that they can attend the AGMs to raise issues.

There are other pieces of legislations which support the Companies' Act, such as the King III, which contains provisions that uphold shareholder rights.

6.5.5 Governance related issues

Governance related issues identified by the respondents. Governance related issues identified by PwC (2015) are: board that do not meet best practice expectations and have different governance profile to that of their peers. Board compositions and the length that board members have served on boards fall under board practices. The most contentious issue under governance related issues is the remuneration of executive directors: the disclosure of the remuneration policies which is discussed under section 6.5.3: Non-disclosure of key information.

In summary: research question 4

Out of the five key drivers identified by the respondents, only one, performance, is supported by the literature review in Chapter 2. This could mean one of the two things: the other three (use of excess cash in the business, non-disclosure of key information and changes in legislation) are not applicable to South Africa, or these drivers are fairly recent and have not found their way into academic literature as yet.

Non-disclosure and changes in legislation have been strongly supported by evidence which emanated from the interviews. The use of excess cash in the business has been mentioned by those companies which are exposed to hedge funds in their shareholding.

6.6 Research Question 5

What are the common demands made by shareholder activists in South Africa?

Four main shareholder demands were identified: namely, executive remuneration, request for information, control of unissued share capital, and directors' governance matters. Two of these, executive remuneration and request for information, have been identified as common to both this research question and research question 4 for key drivers. As a result, they have already been discussed extensively by the researcher.

Surprisingly, this demand came up frequently in the responses. The new Companies Act, 2008 gives an additional right to directors of a company, they can without prior approval of the shareholders issue shares using their discretion. There are only two provisions which they have to meet. The first one is they can issue these shares provided the share issues are made within the classes and secondly, the shares in have to have been authorised by or in terms of the memorandum of incorporation of the company. Shareholders have concerns that directors may dilute their shareholding by selling off the authorised unissued share capital without their consent.

In terms of corporate governance-related demands, four sub-themes emerged from the data, namely, the removal of directors from office, independence of directors, tenure of directors in office, and lastly, the attendance record of board members. Gantchev (2013) identified the election of shareholder activist nominees to the board of directors; the removal of certain board members; and the replacement of management as the most common demands made by activists shareholders to corporates.

The mandate of the board is to act in the best interest of the company, but sometimes that is not the case. In some instances, the boards fail in the fulfilment of their mandates or, in fulfilling their mandates they go against shareholders' demands. The trend observed in these instances is for shareholders to call for the removal of the board.

The question of the independence of the board came up several times as a favourite. Shareholder activists also questioned the tenure of some directors and linked the length of service to their independence or perceived lack thereof.

In summary: research question 5

The interview findings as they relate to the most common demands that shareholder activists make to South African boards were slightly different to the ones evidenced from the literature review. The only shareholder demand that appear in both literature and the empirical findings is the demand pertaining to governance-related issues, which includes executive remuneration.

The issue of authorised unissued share capital is unique to South Africa. Perhaps, although the relationship between the boards and the shareholders leans toward stewardship theory, there could be deep-rooted trust issues between the two.

6.7 Research Question 6

What are some common strategies used by activists to realise their demands?

The main themes that emerged as common strategies employed by shareholder activists in realising their demands include the following:

- Direct communication with management or the board
- Lobbying of other shareholders
- Attendance at the AGM
- Use of public media platforms.

According to the responses, many shareholder activist spend time behind the scenes negotiating with the companies they have invested in to reach consensus around key strategic initiatives to unlock and improve value. Some of the corporate governance flaws discussed this way as a method to safeguard the value in the businesses. Some of the most persuasive strategies used by shareholder activists are lobbying of other shareholders and using the media to achieve their objectives (Girard, 2011). According to the respondents, shareholder activists also spend time talking to some of the company's other shareholders to assess their thinking around the planned changes.

In summary: research question 6

The interview findings as they relate to the strategies used by shareholder activists in South Africa to realise their demands were consistent with the findings evidenced from the literature review. Activism can take many forms, and shareholder activists have

several avenues of approach at their disposal. Shareholder actions evolve and can turn into stronger action or get diluted.

6.8 Research Question 7

How do South African boards respond to shareholder activism?

Most South African companies are open-minded in terms of shareholder activists' demands, and engage proactively. The boards often engage in direct dialogue with the shareholder activists and accommodate most of their demands. In instances where the activists' demands cannot be accommodated, the board goes to great lengths to indicate to the shareholder activists that their demands were given due consideration.

6.8 Research Question 8

What is the role of corporate boards in dealing with shareholder activists?

The role of South African boards in dealing with shareholder activists has three components, as follows:

- To objectively consider the activists' demands or ideas
- To actively engage with the company's major shareholders
- Statutory duties.

The responsibility of corporate boards in dealing with shareholder activists is to objectively consider the activists' demands irrespective of the nature thereof. The respondents believe that by the time the activists approach the company, most of them have genuine concerns about the company that need to be addressed or have developed strategies to enhance shareholder value.

If the board does not believe that the activists' demand are in the best interests of the company, their responsibility is to communicate this to the shareholder activists and to explain how the board came to reach that conclusion. In objectively considering activists' ideas and ideas, the board's role is to proactively engage in direct dialogue with the shareholder group (Cossin & Cabarello, 2013).

According to Logsdon and Buren (2009) there are benefits in boards engaging shareholders directly. Firstly, direct engagement indicates that the board takes the

shareholder relationship seriously, while secondly, these dialogues often result in the sharing of ideas and convergence of expertise.

The third role of the board in terms of shareholder activists is to bear in mind its statutory responsibilities. The board's responsibilities are embedded in the legislation (Companies Act, 2008) and King Code of Corporate Governance. The role of the board is to look after the interests of all its stakeholders but ultimately to act in the best interest of the company.

In summary: research question 8

The interview findings as they relate to the role of corporate boards were consistent with the findings evidenced from the literature review, with the exception of the statutory role which is unique to the South African environment as a result of the King III Code of Good Governance and the Companies Act, 2008.

The board of directors has a number of decisions to make in its responses to shareholder activists. It can acquiesce with shareholder activists' requests, compromise with these activists, or reject and defend the decision to do so.

A review of the legislation above indicated that directors have a responsibility to all stakeholders, including shareholder activists. This was also supported by empirical evidence gathered during the interviews, as reflected in Chapter 5.

The findings furthermore revealed that the directors are cognisant of the fact that as the top decision-making body of their organisations, their role is to look after all the stakeholders. They are therefore instrumental in ensuring that the demands of the shareholder activists are given the time and platform they deserve.

6.10 Research Question 9

How do corporate boards prepare for shareholder activism?

There are two main components to preparing for dealings with shareholder activists by companies in South Africa, namely monitoring of the company's ownership, and developing an engagement plan that is tailor-made to the company's shareholders and the critical issues in the organisation.

The data analysed indicated that companies have developed plans to deal with shareholder activists. Activists, according to the respondents, normally engage with both members of the board and management and the plans include both engagements at these levels.

Companies, in preparing for shareholder activism, seek an understanding of the shareholder base and the shareholders' key objectives. They look at the profile of each shareholder and the kind of issues they are likely to raise and the steps they may take. As part of the preparation, companies need to understand the type of shareholder they are dealing with and the sorts of demands these shareholders are likely to raise (PwC, 2015).

In most instances, companies have dedicated investor relations departments made up of senior enough senior personnel who are able to deal with most of the shareholder demands and/or redirect them to relevant people in the organisation. According to Atkins (2013), companies should also have a dedicated investor relations team customised for each shareholder demand and the type of shareholder ready to deal with shareholder issues as and when they arise.

There is furthermore a history of ongoing engagements with shareholders starting with results roadshows and material decisions that the company needs to make. These roadshows are directed to significant shareholders and are aimed at helping shareholders have a better understanding of the company and of how the directors are fulfilling their oversight responsibilities. This also reduces the agency costs in organisations.

In summary: research question 8

As indicated in Chapter 2, the academic literature addressing research question 8 does provide direction in terms of the strategies that the board of directors needs to follow to prepare for shareholder activism (The literature under that section comes from industry experts, as little published literature was available on the topic).

The directors are cognisant of the fact that preparation for shareholder activism is an integral part of their duties as directors. There is consensus among directors that the company needs to develop a shareholder engagement plan to deal with all the issues on which shareholders would like to be appraised. Clear, simple and concise communication is vital.

6.11 Linking empirical evidence to academic theory

The empirical findings and literature review demonstrate that the shareholder activism landscape in South Africa depends on the relationship among several of the governance role players. The relationship factor introduces the agency and stewardship theories to the mix. Daily and Canella (2003), in support of agency theory, argue that shareholder activism is designed to reduce managers' self-interest by coercing managers with incentives to implement practices that safeguard the interest of shareholders. It is, however, evident from the empirical data that boards of directors in South Africa are more likely to acquiesce to shareholder activists' requests and are much more collaborative than their counterparts elsewhere in the world.

It can thus be deduced that the shareholder activism model in South Africa cannot be fully attributed to the principles of the agency.

Cornelius (2005), in explaining the principles of stewardship theory, indicated that directors, left on their own, will act responsibly towards the assets they control, therefore minimising the need for shareholder activism on the part of shareholders. The empirical evidence indicates that South Africa is not quite there yet. The research concludes that the South African shareholder activism model as perceived by company directors is somewhere in the middle of the road in terms of either following the agency or stewardship theories of management.

6.12 Conclusion

The key findings of this study are that the type of shareholder activism prevalent in South Africa is corporate governance activism in nature, focusing on the firm's governance reforms. It is driven by large institutional shareholders who are interested in safeguarding the value of their investments. These institutional shareholders prefer to raise their demands or contentious issues with directors behind closed doors or across the table so to reach an amicable solution. Lobbying among each other in order to reach consensus is another favoured strategy. Very few value players raise critical issues in the public domain.

Conversely, boards of directors are more collaborative to shareholder activists' demands, and are likely to accede to these or go to great lengths in an attempt to demonstrate that they have been given due consideration in cases where they do not accede.

The directors overall are certain that shareholder activism is valuable and integral to the principles of good corporate governance, and that the long-term benefits of activism far outweigh its shortcomings. They emphasised the role of open and transparent communication and disclosure among key stakeholders as crucial to the relationship. The importance for shareholder activists to possess the right level of knowledge of the organisation was stressed in order for them to avoid raising unreasonable demands and to add value to the relationship.

CHAPTER 7

CONCLUSION

7.1 Introduction

The purpose of this study was to explore the perspectives of South African directors as they relate to several key factors of shareholder activism. Incidences of shareholder activism have definitely increased in South Africa of late, and shareholders are much more powerful and involved than in previous years.

The country has furthermore made a fundamental shift both in shareholder and director sentiments. Shareholder activists are no longer seen as corporate raiders who are there to extract as much value as possible from the companies in which they have invested, but rather, are viewed as authentic investors seeking increases in shareholder value. Corporate boards and directors can no longer do as they please and are much more accountable to shareholders than before.

This chapter presents the final argument of the research presented therein, summarising the main findings. It also sets out the academic and managerial implications of this study, highlighting the contributions made to the literature and the implications for businesses.

7.2 Main findings and conclusions

The key finding of this study revealed that shareholder activism was identified as crucial to improved governance within companies. Issues not dealt with previously are now being brought to the boardroom table and dealt with properly. Directors perceive shareholder activism as a process that enhances value and improves ways in which companies do business in South Africa.

As a result of shareholder activism, companies now have improved governance in place, as well as transparency and improved disclosure. Issues which are now raised are no longer limited only to performance but to the economy as a whole, such as BEE and compliance thereof.

The findings validated the role of directors, as this relates to shareholder activism, is to act in the best interest, of the company. Many directors believe that they have a responsibility to treat all stakeholders in an equitable manner. This implies that they have to consider requests from all shareholders, which include those of the activists, and deal

with them in a manner that is acceptable to all. Building of good working relationships has been highlighted as crucial to dealing with shareholder activists. Moreover, sharing of information helps with the building of these relationships.

Another critical finding addressed the ways in which directors manage and prepare for shareholder activists, and found that collectively, directors contributed the most efficient ways to prepare, anticipate and to “activist-proof” their organisations. Activist-proofing in this context means that the organisations minimise the negative sentiments of shareholder activism mentioned earlier in the study.

A guideline below has been compiled by combining various findings of the study herein. The guideline is designed to assist directors to effectively prepare, respond and manage shareholder activism. This guideline will also assist in building on existing literature.

7.3 Additional findings

The results of the study confirmed that shareholder activism goes through different phases, and the nature and intensity of it depends on who the driver is and what strategies they employ. A case in point was made regarding the Public Investment Corporation (PIC) in terms of the various strategies the PIC employs in terms of shareholder activism. The PIC is a significant shareholder in most listed companies on the JSE and the largest institutional shareholder in South Africa. The findings revealed that the strategies employed by the PIC to realise some of their demands set the tone and landscape for shareholder activism in South Africa. These strategies evolve, depending on who is sitting at the head of the organisation.

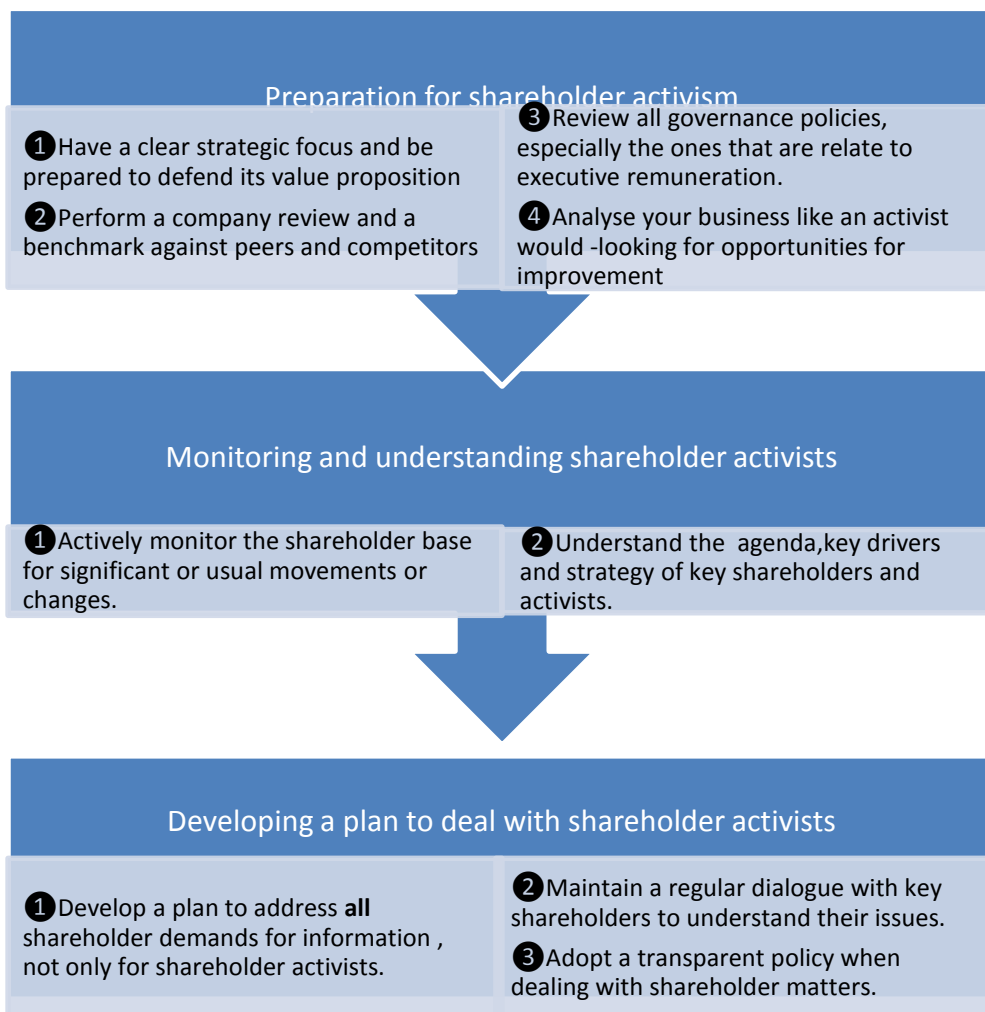
The second additional finding pertains to the huge and complicated changes that South Africa has gone through in the recent past. The findings of this study indicated that directors believe shareholder activists need a proper understanding of the complexities brought about by the changes in South Africa. Examples of these are remuneration, BEE and transformational issues. Proper understanding of all these pertinent issues ensures appropriate handling of shareholder activism issues in a manner that is complimentary to the company.

The last finding here revealed that corporate activities in terms of hostile mergers and acquisitions have not been prominent in South Africa for various reasons. Firstly, the regulatory requirements and approvals required to acquire a company in South Africa are quite onerous. That on its own makes it difficult without putting the additional burden

of sellers and/or management who are not willing to cooperate. The risk that the hostile takers need to assume is very high. Secondly, the size and nature of shareholders in the country serves as a deterrent in terms of the harsh or forceful nature of shareholder activism. Hostile takeover activists often find themselves without the backing of large institutional shareholders in the country. This relates to the risks that these shareholders are willing to take.

The findings of this study confirmed that there was a need for this research as the literature did not fully address some of the key elements of shareholder activism. This was evident in the empirical findings, as the directors affirmed the lack of clear guidance from literature in preparing for and pre-empting shareholder activists.

Figure 1: Proposed guideline: directors effectively preparing and responding to shareholder activism



7.4 Academic implications

The main contributions to the literature presented herein are twofold. Firstly, the study provides a better understanding of shareholder activism in South Africa and in an emerging and developing economy to minimise the impact. It clearly defines shareholder activism as understood and lists the type of shareholder activists and the most common demands. Three of the four common demands that shareholder activists make could not be predicted from the literature and emerged as unexpected. These will now add to the academic literature within this field. Secondly, the study contributes to the potential drivers and key strategies that underpin the existence of shareholder activism in the country. The researcher attempted to clarify certain aspects of shareholder activism to arrive at academic conclusions that may be used as hypotheses for further academic research. Lastly, the literature was not adept in addressing the different defence mechanisms that directors need to employ in order to manage and address shareholder activism. The study contributed by devising a framework to address that gap.

7.5 Business implications

The study of shareholder activism contributes significantly to building a better understanding of dealing with shareholder activists in South Africa. It has brought to the fore the levers for directors to manage shareholder activism within their companies. Directors can now build a better understanding of the moves available to them. These could include pre-empting potential shareholder activists' actions or demands through mechanisms put in place as a result of the framework developed in the study.

With regards to the response to shareholder activism, it is important for directors to understand that not investing in building relationships with shareholders, especially shareholder activists, could result in unreasonable demands from said shareholder activists, as well as the company not benefitting from the positive aspects of shareholder activism and negative publicity. This adversarial relationship can be prevented by adopting a more relational and accommodating approach to shareholder activists.

An organisation that is constituted of shareholder activists, as in the case in other markets like the UK, USA and Australia may result in more focused and targeted issues being canvassed in the future.

7.6 Limitations

Despite the contributions mentioned in the report, the study does carry some inherent limitations associated with the research methodology used. The limitations were mentioned in Chapter 4 and but for ease of reference will have been listed again below:

The following limitations were identified in conducting the research:

- Not many companies could differentiate between shareholder activism and shareholder engagement, making it difficult to obtain data. Interpretation of the research topic is a challenge. Saunders and Lewis (2012) warned of an impact in research methodology when a researcher has to adapt to accommodate different interpretations of the topic or study by the interviewees.
- Interviews for exploratory interviews were time-consuming and may have deterred participants from taking part in the interview process.
- The use of non-probability sampling resulted in a non-representative sample.
- Interviewers did not discuss the negative aspects of their principal-agent relationship due to the fear of reprisals.
- Exploratory research was performed to gain insight into a new phenomenon and does not provide definitive conclusions (Saunders and Lewis, 2012).
- The use of an occasional spontaneous question in an exploratory interview made quantifying and analysing the answers difficult.
- The use of spontaneous questions on some respondents and not others could be seen as unfair or possibly misleading.
- The interview process required skill to avoid generalisations and possible bias.

7.7 Recommendations for future study

The first step to be taken in any future research is to perform an empirical validation of the findings by using qualitative research methodology. Qualitative research will also assist in addressing perceived short-comings in the literature reviewed.

The researcher proposes the following areas for further study within the field of shareholder activism:

- Most big South African corporates have common shareholders; a further study could test the impact of that on shareholder activism.

- The research only looked for views of one stakeholder group, namely directors. A further study could test the views of other stakeholders.
- A further study could test all the other aspects of shareholder activism mentioned in this report, such as key drivers, common demands and strategies used by shareholder activists.

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Appendix A Interview guide

The gathering of data from the directors was conducted using in-depth semi-structured interview technique. The questions below were expected to generate a discussion of approximately five minutes of the topic. The average interview time was forty five minutes.

1. Please state your name and position
2. What is your understanding of shareholder activism in the context of your company or in South Africa? Who are these shareholder activists?
3. How do you perceive the existence of shareholder activists? Do you believe they enhance governance structure or a disruption to management in running their companies? Do you think they add value or destroy value for the companies?
4. What, in your opinion, are the key drivers of shareholder activism in South Africa?
5. What are some of the demands made by shareholder activists in your company?
6. What issues have been elevated to your boardroom agenda as a result of shareholder activists' demands in the last 3 to 5 years?
7. What strategies are used by activists to realise these demands?
8. In your opinion, what should be role of your board in dealing with shareholder activists?
9. What has been the response of your board to shareholder activists' demands in the past?
10. Does your company prepare for shareholder engagements in advance? Please elaborate on your answer.
11. In your expert opinion, how should companies prepare for shareholder activism?
12. What are your personal views on shareholder activism and its effect in South Africa in the past decade?
13. Any other aspects that you believe that should be considered under the title of shareholder activism?

Appendix B Interview Consent form

I am conducting research on the perspective of directors on shareholder activism in South Africa. The interview is expected to last an hour, and will help us gain understand how South African directors and boards anticipate, react and deal with shareholder activism. Your participation is entirely voluntary and you can withdraw at any time. All information obtained from this interview will be treated as confidential, all data will be stored without any identifier whatsoever and only the researcher will know your name and name of the company.

The contents of the interview may be made publicly available, in the form of an MBA thesis without your name, position, organisation or any identifiable details. If you have any concerns, please feel free to contact me or my supervisor, whose details are provided below.

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Name of participants: _____

Signature: _____

Name of researcher _____

Signature: _____

Date: _____

