

# The rise of passive investing and activism, ESG, Brexit and political uncertainty

Not only is the UK in the midst of political turmoil, the global economy is also changing significantly. **James Jarvis** looks at the seismic shifts in the corporate world, and what you can do to avoid becoming extinct.

Darwin once remarked that the survival of a species was not down to strength or even intelligence, but due to the ability to adapt to change. Likewise, businesses who are best able to adapt to the maelstrom of change today are the ones most likely to be around tomorrow.

These changes range from macro headline issues, such as Brexit and climate change, through to nitty gritty regulatory changes and the evolving nature of investment, all of which are presenting new dynamics for boards to grapple with.

## Multifaceted and uncertain

Starting with the B-word, here the potential for disruption is as multifaceted as it is uncertain. While the word itself has been echoing through Whitehall and boardrooms for what feels like an eternity, whatever the end reality actually is will have an affect not only on organisations' operational endeavours, but also on the

regulatory environment they sit within. With the City of London's crown no longer guaranteed and with jurisdictions across Europe and beyond vying for the throne, there is a knock-on risk to the UK's hard-won position as a leader in governance standards and investor protections.

## Relaxing of rules

As was seen in the recent move to alter listing rules for sovereign controlled companies here in the UK, there is always the temptation to tinker with standards in order to attract new business. Regulatory 'loosening' is already occurring in other jurisdictions in a bid to woo issuers; Hong Kong and Singapore have relaxed their 'one share one vote' requirements, and over in the US the Trump administration is also making overtures to business via the removal of regulation.

While a shift in such fundamental tenets of investor rights may seem impossible in the UK, the temptation to

## THE RISE OF ACTIVISM

- 85% of UK investors say they are willing to work alongside activist investors.
- Activists are increasingly using corporate governance as a tool to achieve their aims.
- Activism is on the rise in Europe.
- A company's governance and equity story is only as convincing as the underlying framework on which it rests.

cede to the demands of the next generation of companies could prove irresistible.

## Changing investor climate

Meanwhile investors themselves are feeling the spotlight shift onto them after several years in which regulators and policy makers have been fixated on the board. The launch of the revised Stewardship Code in the UK will increase the pressure to evidence both the actions and results of investment stewardship. In addition, mirroring developments we have seen on the Continent, culture and purpose have found their way across from the main code and feature throughout the proposed document.

This comes at a time when two distinct schools of investment are both growing and converging – the passive index fund and the activist hedge fund.

Activist activity in Europe has been heating up over the past few years and it is perhaps the changing nature of both the tactics deployed and the size of the companies targeted that is interesting to observe. The language of corporate governance is being increasingly used alongside the usual financial focus on shareholder value and huge household names are finding themselves to be fair game for such approaches.

In addition, the clear willingness of other investors to work alongside these



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funds (some 85% according to the latest annual Edelman Institutional Trust Barometer) shows the changing market perception of the 'corporate raider'. Faced with their superior returns to more classic investment strategies, passive funds regularly invest a portion of its active investment with activist investors.

While other investors may be showing a propensity to work with or indeed mirror some of the tactics of activists, policy makers on the continent are waking up to this perceived 'threat'. France recently announced they would be investigating activist funds and other jurisdictions could well follow suit.

**Trillion-dollar investors**

On the other side of the coin, while the index fund is often heralded as one of the greatest innovations of modern finance, the exponential growth of their size and influence is also beginning to cause concerns in some corners as its advent has created the "Trillion-dollar investor class".

Even the late John Bogle, the father of the index fund, in his later years questioned the wisdom in a foreseeable scenario where a small concentration of these funds have such an influence over so much of our equity markets.

**Use the right tools**

Handling these multiple and often interlinked changes are company directors and those that serve around them. How they incorporate the differing priorities of distinct investment approaches, react to regulatory changes and embrace the opportunities which tomorrow brings will in large part define whether the companies they work for will survive into the next decade and beyond.

Obvious though it may seem getting the strategic, commercial and financial basics right will equip companies with potent tools to do just that.

Company purpose, organisational culture and the values that underpin all of these are coming of age in corporate discourse and marrying these with your strategy is as good a start as any to deal with forthcoming change.

A company's governance and equity story is only as convincing as the underlying framework which assures it. Once in place it is far easier to convince stakeholders of the merits of any necessary adaptation. ■

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