MINORITY SHAREHOLDERS WATCH GROUP
BADAN PENGAWAS PEMEGANG SAHAM MINORITI BERHAD
(Incorporated in Malaysia – Registration No.: 200001022382 (524989-M)

The Edge Malaysia – Monday, April 4, 2022 **(A)**

Bolstering minority shareholder activism

MY Say

BY WAN NORDIN WAN HUSSIN

Shareholder activism refers to the efforts of investors to exercise their rights as owners to discipline boards and top management teams. It is about driving change, and arises when shareholders believe that the boards have failed to perform their duties, leading to shareholder dissatisfaction with board performance and shareholder value maximisation.

By voicing their concerns and making their dissatisfaction known, either via dialogues, in letters written to the company, through shareholder proposals, by adverse voting, press campaigns or exiting the company, shareholders can influence the practices and strategy of a company. Shareholder activism may include institutional investors' private engagement with companies on issues related to the business model, financial performance, long-term strategic plans and environmental, social and governance (ESG) standards, or retail investors' shareholder proposals, which mostly cover issues related to the board, executive compensation and ESG matters (including auditor-client relationship), as well as hedge funds' campaigns to put the company, or part of the company, up for sale.

The mid-1980s saw a rise in shareholder activism when institutional investors such as pension funds, asset managers, mutual funds and insurance companies became activist investors. A milestone in 1985 was the founding of the Institutional Shareholder Services and the Council of Institutional Investors in the US. These activist institutional investors initiated shareholder proposals, pressured management "behind the scenes" and used public media campaigns to target the boards and senior management of poorly governed or underperforming companies to implement corporate reforms.

In the 1990s, labour union pension funds replaced public pension funds as the main shareholder activism player, and mutual funds also jumped on the activism bandwagon. The latest actor to enter the activism stage in the late 1990s was the hedge funds and private equity funds that took large, relatively long-term positions in underperforming companies.

In many cases, hedge fund activists deploy confrontational tactics, ranging from publicly admonishing incompetent executives to unseating the entire board, to achieve their agenda. Thus, hedge fund interventions can induce intense conflicts over firm strategies and often heated battles for corporate control between hedge fund activists and the target firm's management.

There is ample scholarly research around the world that shows shareholder activism is likely to be detrimental to management but beneficial for shareholders. For example, activism is associated with decreased CEO pay and increased disciplinary CEO turnover, but also leads to divestitures of underperforming assets and positive excess stock returns, and improved corporate tax efficiency.

An emerging stream of literature also shows that the threat of activism may elicit greater disclosure of climate risk information. Another positive outcome of activism can be observed with BlackRock's annual Dear CEO letter (published on its website), which compels portfolio firms to align themselves with BlackRock's preferred strategies.

Shareholder activism can also trigger shareholder proposals requesting firms to provide information on corporate political spending, arising from concerns that political spending is symptomatic of agency problems within firms.

In sum, the research findings suggest that exposure to shareholder activism is an important determinant of responsible corporate behaviour, and that targeted firms increase public disclosure to satisfy activist demand or to repel activist advances. For example, managers under threat from activist investors can avoid shareholder activism by increasing voluntary disclosure of earnings forecasts, which corrects mispricing and potentially reduces returns to activism.

In Malaysia, minority shareholder activism is spearheaded by the Minority Shareholders Watch Group (MSWG). The Malaysian government institutionalised shareholder activism by creating the MSWG in 2000, following the 1997/98 Asian financial crisis. The MSWG was initially funded by several domestic institutional investors to create awareness among minority shareholders of their three basic rights — to seek information, voice opinions and seek redress in cases of corporate misconduct and shareholder expropriation. The mission statement of MSWG is to increase sustainable shareholder value in companies through engagement with relevant stakeholders, with a focus on minority shareholder interests.

In the past, shareholders in Malaysia were slightly hesitant to take legal action against boards, challenge those in authority and engage in public confrontation due to cultural factors, such as high power distance and low individualism. Given the high power distance and collectivistic society in Malaysia, a watchdog is an ideal solution, since shareholders who are uncomfortable with confrontation need not fear the board as the provocative issues are raised on their behalf by the MSWG. As a watchdog and gatekeeper that protects the interests of minority shareholders, MSWG monitors the monitors. Its activities include providing voting advice and proxy services, influencing the decision-making process in public-listed companies (PLCs), monitoring corporate governance transgressions, and educating and alerting retail investors by scrutinising and questioning decisions made by companies that are detrimental to the minority shareholders group.

As influencers, MSWG periodically highlights issues in the media and at general meetings for board clarifications. Over the years, MSWG has evolved into an independent research organisation. MSWG selects the portfolio of target companies for monitoring based on certain criteria: (i) companies that are FBM KLCI constituents; (ii) companies that are included in the MSWG's Top 100 Malaysian Corporate Governance Index; (iii) companies that MSWG subscribers request to be monitored; and (iv) companies that warrant monitoring based on complaints received. MSWG also purchases shares in hundreds of PLCs with significant institutional and foreign ownership to enable it to participate in shareholders' meetings. The MSWG's 2020 annual report reveals that in that year, it covered 300 PLCs in its monitoring portfolio, or about 33% of the total number of companies listed on Bursa Malaysia, comprising large-, mid- and small-cap stocks that represent about 87% of Bursa's total market capitalisation.

MSWG's modus operandi is it uses the shareholder general meetings as platforms to raise issues of concerns and encourage or urge actions on good corporate governance and sustainability practices to be adopted by PLCs. By and large, PLCs present their responses to MSWG's letters at the annual general meetings (AGMs), and many include MSWG's questions and their responses on their corporate websites under the Summary of Key Matters Discussed at AGMs.

Anecdotal and empirical evidence suggests that MSWG plays an important role in lifting the standard of corporate governance in Malaysia. One of MSWG's early successes was in preventing minority shareholder expropriation when it played a leading role in aborting the attempted acquisition of Malaysian Merchant Marine Bhd by Maruichi Malaysia Steel Tube Bhd, a deal many saw as a disadvantage to the minority shareholders of Maruichi in 2002.

More recently, MSWG joined forces with the Employees Provident Fund, the largest institutional investor in Malaysia and chair of the Institutional Investors Council Malaysia (IICM), to bring corporate governance reforms in Sapura Energy Bhd. "We oppose the re-election of the independent directors because every year we keep seeing the same thing happening, especially with the excessive director remuneration" (*The Edge*, July 18, 2018).

In addition, MSWG, together with the Securities Commission Malaysia, was instrumental in the formulation of the Malaysian Code for Institutional Investors (2014) and the issuance of the AGM Corporate Governance Checklist for Shareholders (2020), which highlights questions for shareholders to consider in preparation for an AGM. The role of MSWG as a gatekeeper in reviewing the standard of corporate governance of PLCs has been acknowledged by Asian Corporate Governance Association (2020). "The MSWG's continuing role is particularly notable. The organisation provides questions in advance of AGMs and companies frequently include these and responses as an addendum to the company presentation at the start of the Q&A section of the meeting. The consistent assessments have improved the quality and professionalism of AGMs over time in Malaysia."

Moreover, empirical studies show that firms targeted by MSWG elicit more transparent disclosure, more credible financial statements and higher returns. Similarly, a study on the China Securities Investor Services Center (CSISC), the equivalent of MSWG, shows that firms in China monitored by CSISC report lower earnings manipulation, particularly among firms with weaker corporate governance.

Apart from closely following MSWG and IICM's corporate engagement, how else can the investing public better gauge the intensity of shareholder activism among the listed companies in Malaysia? As a way forward, I would humbly suggest Bursa revamp its corporate announcements database under the category of general announcements by adding a sub category that is dedicated to shareholder proposals.

Additionally, Bursa may want to revamp the way the voting outcomes at shareholder meetings are announced by showing separately shares voted under the public float category, as the number of shares held by minority shareholders that voted at the AGM is a good indicator of minority shareholder activism. Under Paragraph 9.19(7) of the Bursa Malaysia Main Market Listing Requirements, the AGM voting results are required to be announced to the public immediately after the meeting. Unfortunately, the voting results in Malaysia only disclose the number of shares voted by all shareholders without distinguishing between shares voted by controlling shareholders or blockholders and those by minority shareholders (retail investors and institutional investors without board representation). A hybrid shareholder meeting, with video streaming and availability of the minutes online, may further bolster the shareholder activism momentum. E

Wan Nordin Wan Hussin is professor and deputy dean (academic and international affairs) at the Othman Yeop Abdullah Graduate School of Business, Universiti Utara Malaysia Kuala Lumpur Campus