AN FTI CONSULTING REPORT – PUBLISHED 3/31/2021

The Activism Vulnerability Report

Q4 2020

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Introduction & Market Update

FTI Consulting's Activism and M&A Solutions team welcomes our clients, friends and readers to our sixth quarterly Activism Vulnerability Report, documenting the results of our Activism Vulnerability Screener from the recent fourth quarter of 2020, as well as other notable trends and themes in the world of shareholder activism and engagement. Almost one year ago to the day, we sat down to write this report for the fourth quarter of 2019. Our team had just begun the shift to working from home offices and spare bedrooms, while still adjusting to full days of video conference calls due to the rapidly spreading COVID-19 coronavirus.

While it was not until the latter half of the fourth quarter of 2020, or even the start of 2021, that many of the pandemic's biggest concerns began to subside, many areas of the market remained incredibly resilient throughout the year. The S&P 500 Index, the Dow Jones Industrial Average Index and the Nasdaq Composite Index rose 16.3%, 7.3% and 43.6%, respectively, in 2020.[1] While the three leading indices all ended the year on solid ground, the incredible market voracity from the COVID-19 pandemic should not be overlooked. The S&P 500 Index reached an all-time peak of 3,386 on February 19, before it fell 33.9% in just 32 days to 2,237. As measured from March 23, 2020, however, the Index regained the previous high in less than five months on August 18 (an increase of 51.5%).[2] For the S&P 500 Index and the Nasdaq Composite Index, the period of 2019 and 2020 represents the best two-year performance since 1998 and 1999, during the heart of the Dot-Com boom.[3]

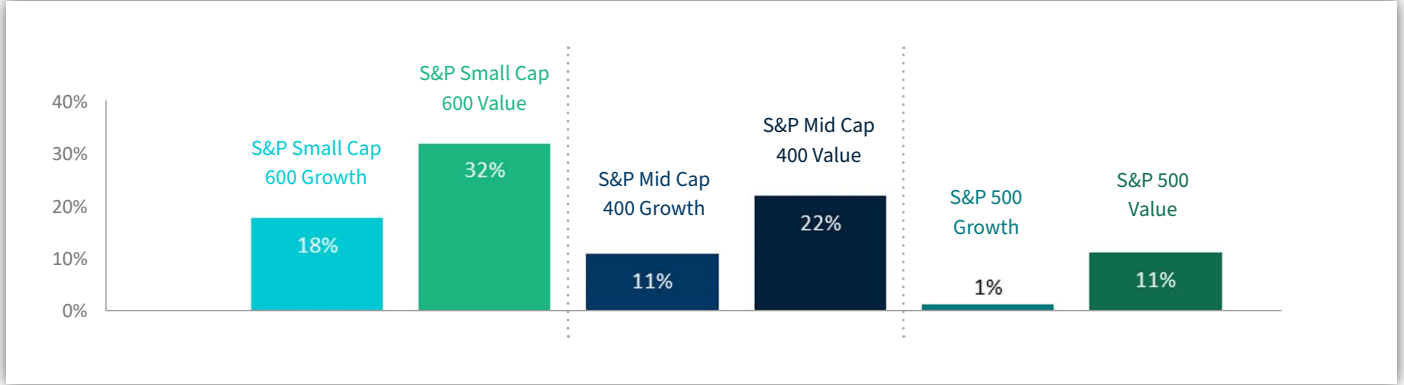
Two Year Performance (2019 and 2020)

2020 was largely a continuation of the bifurcation of the "Growth" and "Value" sectors, with some industries facing outsized pandemic-induced challenges, while others seemed to benefit. The Technology, Consumer Discretionary and Communication Services sectors led the way, returning 44%, 30% and 27%, respectively.[4] On the other hand, the Energy, Real Estate and Financial sectors suffered, returning (33%), (2%) and (2%), respectively.[5] A number of factors led to this "fork-in-the road" performance, including travel restrictions, work-from-home mandates and very low interest rates. Yet, through the first three months of 2021, the opposite has been true. The long-professed rotation out of "Growth" stocks into "Value" stocks may be in process. With the continued rollout of the COVID-19 vaccine and the relaxation of travel and work restrictions, the Organization for Economic Cooperation and Development has forecast the U.S. economy to expand by 6.5%.[6] Historically, cyclical, "Value" stocks (including Energy and Financial companies) tend to outperform during such a recovery period. Alternatively, "Growth" stocks, which performed so well during the low-interest rate era, would become less attractive to investors in a higher-interest rate environment.

[1] FactSet; Proprietary research by FTI Consulting
[2] https://www.oaktreecapital.com/docs/default-source/memos/2020inreview.pdf
[3] https://www.wsj.com/articles/global-stock-markets-dow-update-12-31-2020-11609410021?mod=searchresults_pos2&page=15
[4] FactSet; Proprietary research by FTI Consulting; Performance data from the representative S&P Select Sector Index
[5] FactSet; Proprietary research by FTI Consulting; Performance data from the representative S&P Select Sector Index
[6] https://www.wsj.com/articles/value-investors-finally-have-reason-to-celebratefor-now-11615545000?mod=hp_lead_pos3

From the beginning of 2021 through March 15, 2021, the three S&P 400, 500 and 600 Value Indices had all outperformed their respective Growth counterparts. Moreover, the Energy and Financials sectors have been the two best performing sectors year-to-date, returning 40% and 17%, respectively; the Technology sector was the fourth worst performing sector, up on 2% over the same time-period.[7]

YTD Performance (Jan 1, 2021 – Mar 15, 2021)



It would hardly be a 2020 market update without touching on two of the most prominent (at least within the media) themes of the year: (1) Special Purpose Acquisition Companies ("SPACs") and (2) the rise of the retail investor. In 2020, SPACs were launched by everyone from athletes and celebrities (Alex Rodriguez and Shaquille O'Neal) to prominent business and political figures (Danny Meyer and Paul Ryan).[8] Well known activist investors, including Bill Ackman, Jeff Smith and Daniel Loeb, also took part in the new opportunity to raise funds, giving rise to the phrase "SPACtivism." At the time of offering (July 2020), Ackman's SPAC debuted as the largest-ever "blank-check" initial public offering, raising $4 billion in proceeds.[9]

While each SPAC leverages the expertise of its founder(s), there have been some sectoral themes. In 2020, nearly 70% of SPAC acquisitions were within leading growth sectors, such as Technology, Consumer Discretionary and Health Care; whereas, in previous years, the offering was most frequently used for acquisitions in the Industrial, Financial and Energy sectors.[10]

In 2020, there were 248 SPAC IPOs, which raised, in aggregate, $83 billion of gross proceeds - both records by multiple magnitudes of scale. Through the middle of March 2021, there have already been 275 SPAC IPOs, which have raised, in the aggregate, $88 billion of gross proceeds.[11] Suffice it to say, the SPAC market is set to remain an area of focus in 2021, bringing a substantial amount of new companies to the public markets.

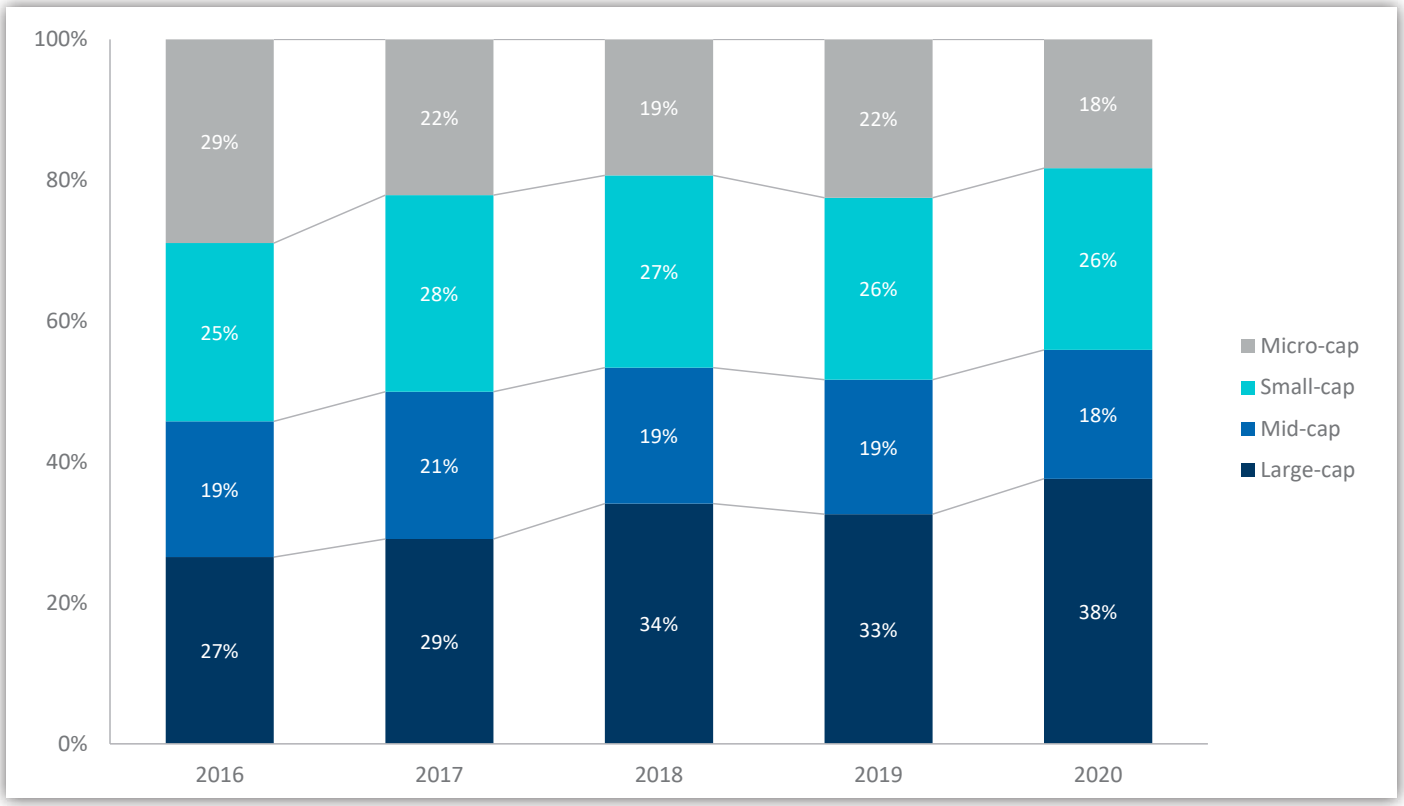
Beyond SPACs, no theme garnered the market's attention quite like the rise of the retail investor. Driven in part by COVID-19 stay-at-home and work-from-home restrictions, many investors/traders spent their free time focused on the stock market. Individual investors opened more than 10 million new brokerage accounts in 2020, also a record. Notably, not only were more retail investors participating in the stock market, they were also doing so much more actively. In 2020, retail investors share of daily total trading volume doubled from 10% to 20%.[12] The significant market events that transpired in January 2021 (*i.e.*, the rise and fall of GameStop, AMC Entertainment and BlackBerry, to name a few) signal a once-ignored market participant seeking an increasingly public voice. What it means for both corporations and institutional investors, when considering newfound methods to engage with retail investors and their role in the shareholder base, remains to be seen.

[7] FactSet; Proprietary research by FTI Consulting
[8] https://www.wsj.com/articles/the-celebrities-from-serena-williams-to-a-rod-fueling-the-spac-boom-11615973578
[9] https://www.barrons.com/articles/bill-ackmans-blank-check-company-starts-trading-today-what-you-need-to-know-51595422200
[10] https://www.wsj.com/articles/stocks-surge-in-crazy-year-for-financial-markets-11609497000
[11] https://spacdata.com/
[12] https://www.wsj.com/articles/new-army-of-individual-investors-flexes-its-muscle-11609329600?mod=series_yearend2020marketsreview

Shareholder Activism Update

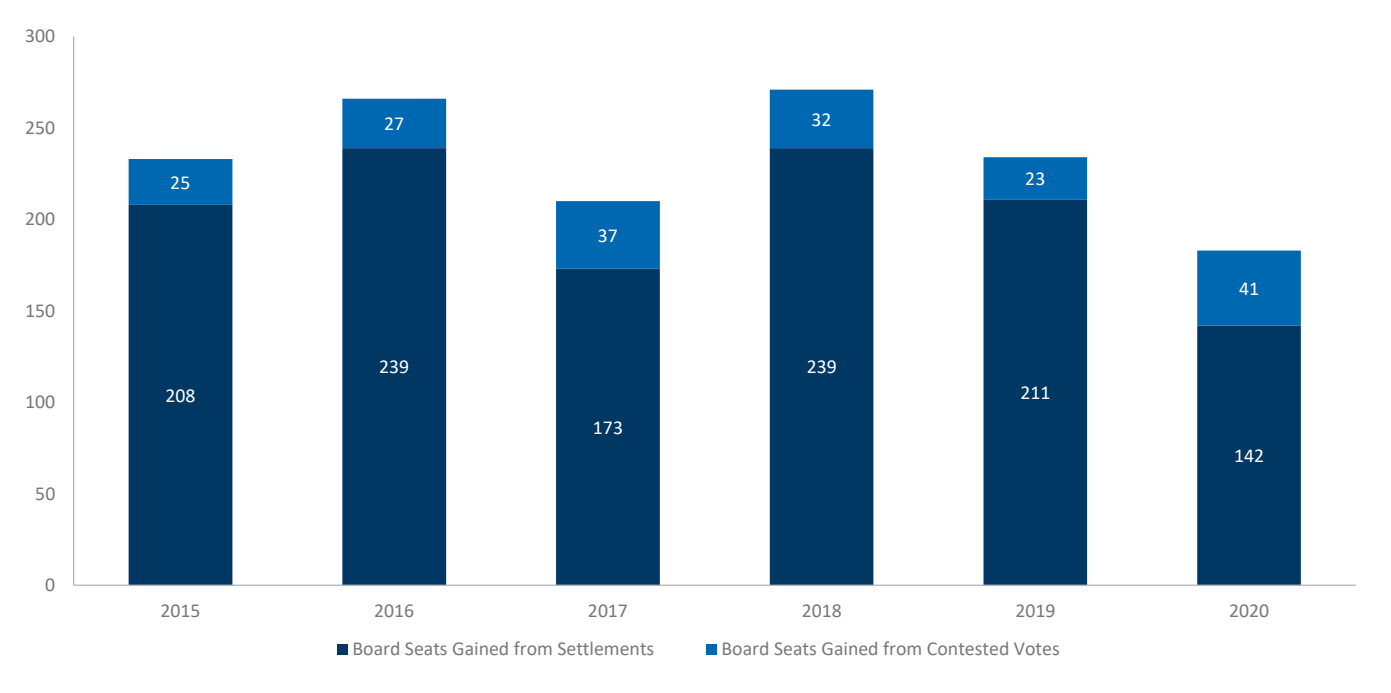
While U.S. shareholder activism was down on a YoY basis in 2020, with U.S. Activist Targets down 9% from 2019 levels, the segment saw new signs of life in the fourth quarter. With 65 new U.S. targets, the fourth quarter represented a 5% uptick in U.S. Activist Targets, compared to fourth quarter levels in 2019 (and was the most active fourth quarter since 2016). The Industrials sector finished the year as the most frequently targeted sector within the U.S., followed by the Technology and Consumer Cyclical sectors. When compared to 2019 activity, the Industrials sector saw the biggest increase in activist attention, while the Consumer Cyclical sector saw the biggest decrease in activist attention, as determined by new targets.[13]

2020 also witnessed the continuation of a five-year trend of increased focus within the U.S. on large-cap (> $10 billion market-cap) activism. Large-cap activism represented 38% of all new targets above $50 million in market-cap in 2020, compared with 33% of all targets in 2019 and 34% of all targets in 2018. The micro-cap (< $250 million market-cap) segment saw the largest decrease within U.S. activism targets in 2020, a relatively consistent trend over the same five-year period. The uptick in large- and mega-cap activism in 2020 is, at least partly, due to the inherent stability of larger, established companies, during a pandemic and a challenging market environment.[14]



Total board seats gained by activists within the U.S. finished the year at the lowest level, by a significant margin, since 2015 (when Activist Insight began tracking the data) and down 22% when compared to 2019. Interestingly, Board Seats Gained in Contested Votes increased substantially in 2020, finishing the year up 78% compared to 2019, with the most Board Seats Gained in Contested Votes since 2015 (when Activist Insight began tracking the data), suggesting that campaigns that went the distance, despite the optics surrounding the pandemic, had more merit.[15]

[13] https://www.activistinsight.com/research/Insightia_ShareholderActivism2020.pdf
[14] https://www.activistinsight.com/research/Insightia_ShareholderActivism2020.pdf
[15] https://www.activistinsight.com/research/Insightia_ShareholderActivism2020.pdf



Beyond the obvious COVID-19 impediments and the challenging market environment, the significant downtrend in U.S. activism campaigns in 2020 was also a result of the historic issuance of shareholder rights plans (a/k/a "poison pills"). U.S. corporations, likely feeling the pressure of their diminished share prices and challenged near-term strategic outlook, employed poison pills to fend off activist investors and hostile acquirers, alike. In 2020, within the Russell 3000, 60 companies issued new poison pills, compared to just 15 in 2019.[16] While the uptick in poison pill issuance was generally understood and accepted by the market, a handful of company have recently seen their provisions voted down, a rare occurrence.

In February 2021, Williams Companies' poison pill provision was struck down by the Delaware Chancery Court, with Vice Chancellor Kathaleen McCormick writing that the pill was "extreme" and disproportionate. Two provisions within the plan warranted particular criticism: (1) the threshold an investor would have to accumulate to trigger the pill was set at an unusually low 5% and (2) a "wolfpack" provision aimed at preventing investors from contacting other similarly minded shareholders.[17] The decision will likely set a precedent for the latitude which both U.S. corporations and legal advisors take in drafting future poison pill provisions.

In the same vein as the downtrend in U.S. shareholder activism, 2020 witnessed a downtrend in proxy fights and contests. Globally, the number of proxy contests that went to a shareholder vote decreased to 88 proxy contests from a record 99 proxy contest in 2019. An interesting voting trend emerged amongst the "Big Three" (BlackRock, Vanguard and State Street), according to Activist Insight. BlackRock increased their support of dissident nominees in 2020 to 25%, compared to just 10% in 2019. Furthermore, all three firms showed an increasing willingness to depart with proxy advisor recommendations when compared to previous years, with State Street and Vanguard voting with recommendations 60% of the time and BlackRock only doing so in half of its votes in 2020.[18]

[16] https://www.activistinsight.com/research/Insightia_AIAR2021.pdf
[17] https://www.reuters.com/article/us-williams-activist-ruling/judge-strikes-down-williams-cos-poison-pill-takeover-defense-idUSKBN2AQ33J
[18] https://www.activistinsight.com/research/Insightia_AIAR2021.pdf

The top activist investors (by capital deployed) for 2020 remained largely the same as in prior years, as brand-name activists continued to deploy capital at large- and mega-cap companies. Elliott Management finished as this year's most active fund with $3.0 billion invested in new campaigns, followed by Third Point Partners and ValueAct Capital, with $3.0 billion and $1.5 billion, respectively. Of note, under the same methodology, the fourth most active investor was Jeff Ubben's new social impact fund, Inclusive Capital Partners, with $1.1 billion invested in new campaigns.[19]

As the activism environment continued to heat-up in the fourth quarter, a handful of brand-name funds and new entrants launched new campaigns, with a majority focused on large- and mega-cap companies. In December, Third Point Partners launched a new campaign at Intel with founder Dan Loeb calling for a strategic review. By early January, Intel publicly announced that it would replace its current CEO, a move which Loeb publicly lauded.[20] In mid-March, Intel's new CEO announced an ambitious $20 billion investment plan for new manufacturing plants.[21] Continuing the trend of fourth-quarter mega-cap targets, the newly launched Engine No. 1, with the backing of the California State Teachers' Retirement System (CalSTRS), wagered a campaign against Exxon Mobil seeking board representation and a shift in capital allocation toward clean and renewable energy; D.E. Shaw launched their own campaign the following week.[22, 23] Amidst the public pressure, Exxon made a handful of ESG improvements, including enhancing carbon disclosure and reducing methane emissions.[24, 25] In March 2021, the company appointed Jeff Ubben (Inclusive Capital Partners; formerly of ValueAct Capital Partners) to the Board of Directors. While D.E. Shaw praised the appointment, Engine No. 1 continued to support its own slate (as of the publication of this report) and stated that Exxon Mobil continued to "resist real change."[26, 27]

Continuing the burgeoning trend of ESG and environmentally focused shareholder activism, prominent activist investor Christopher Hohn of The Children's Investment Fund Management ("TCI") recently voiced his desire for an increase in shareholder proposals. In January 2021, Hohn announced his intention to speed up the process of U.S. companies that publicly disclose their carbon-reduction plans. Hohn and TCI are currently working with certain non-profit groups and investor organizations to convince at least 100 companies within the S&P 500 Index to adopt the initiative by the end of 2022. In discussing his motivation and intention for the campaign, Hohn said, "As shareholders, we can't wait on regulators to solve this. It's on investors to show how seriously they treat this threat."[28] TCI's initiative was launched concurrently with the latest CEO letter from BlackRock's Chairman and CEO, Larry Fink, which pledged to urge companies to improve environmental disclosures.[29] Hohn will ultimately need the support of the "Big Three" if his initiative is to gain momentum in the U.S. in 2021, and beyond. Perhaps the SEC may also lend its support for this initiative under new leadership.

[19] https://www.activistinsight.com/research/Insightia_ShareholderActivism2020.pdf
[20] https://www.wsj.com/articles/intel-ceo-bob-swan-steps-down-11610548665
[21] https://www.wsj.com/articles/intel-ceo-fast-tracks-turnaround-bid-with-20-billion-investment-plan-11616533200?mod=hp_lead_pos1
[22] https://www.reuters.com/article/exxon-shareholders-engine-no-1-idUKKBN28H1IO
[23] https://www.reuters.com/article/exxon-deshaw/hedge-fund-d-e-shaw-pushes-exxon-to-make-changes-cut-costs-boost-performance-sources-idUSKBN28J2JQ
[24] https://corporate.exxonmobil.com/-/media/Global/Files/energy-and-carbon-summary/Energy-and-Carbon-Summary.pdf
[25] https://energyfactor.exxonmobil.com/insights/partners/action-on-methane-regulations/
[26] https://www.businesswire.com/news/home/20210301005315/en/Michael-Angelakis-and-Jeffrey-Ubben-Join-ExxonMobil-Board-of-Directors
[27] https://reenergizexom.com/wp-content/uploads/2021/03/Letter-To-Shareholders.pdf
[28] https://www.wsj.com/articles/british-hedge-fund-billionaire-takes-climate-fight-to-s-p-500-11611842401
[29] https://www.wsj.com/articles/blackrocks-fink-urges-companies-to-disclose-do-more-on-greenhouse-gas-emissions-11611670619?mod=article_inline

Q4 2020's Most Vulnerable Industries

In Q4 2020, FTI's Activism and M&A Solutions practice, in partnership with FTI's Data & Analytics practice, introduced a dynamic scoring model that will adjust the treatment of periodically unavailable data points for individual companies. The adjustment is meant to maximize the model's data integrity. Prior quarter results have been updated to reflect the model update.

The table below shows the Total Vulnerability Scores for the 36 industries:

Rank	▲ Rank QoQ	FTI Industry	Q4 2020 Vulnerability Score	Q3 2020 Vulnerability Score
1	▲ 3	Utilities	61.8	57.0
2	▲ 5	Aviation & Airlines	58.7	56.3
3	▲ 11	Insurance	57.5	52.6
4	▲ 5	REITs	57.5	55.6
5	▼ 3	Power	57.1	62.6
6	▼ 1	Real Estate	56.5	56.8
7	▼ 6	Energy	56.3	65.4
8	▼ 2	Savings Banks	54.4	56.4
9	▲ 4	Pharmaceuticals	54.3	53.0
10	▼ 2	Telecommunications	54.0	56.1
11	▲ 5	Aerospace and Defense	53.7	52.3
12	▼ 9	Media & Publishing	53.7	58.5
13	▲ 2	Financial Conglomerates	53.2	52.5
14	▼ 3	Regional Banks	53.1	53.7
15	▼ 3	Hospitality & Gaming	52.5	53.3
16	▲ 2	Transportation	52.4	47.7
17	▲ 2	Agriculture & Chemical Products	52.4	50.3
18	–	Biotechnology	52.2	52.2
19	–	Industrial Distributors	51.6	51.4
20	▼ 3	Business Services	51.5	52.2
21	▼ 11	Restaurants	51.4	53.7
22	▲ 4	Consumer Finance	51.3	48.9
23	▼ 3	Consumer Non-Durables	50.7	51.1
24	▼ 3	Professional Services	50.5	50.6
25	▲ 4	Healthcare Services	50.0	47.4
26	▼ 1	Banks	49.7	50.2
27	▼ 4	Investment Managers	48.8	50.3
28	▼ 1	Automotive	48.1	48.2
29	▼ 7	Chemicals	47.8	50.4
30	▲ 3	Technology-Software	46.7	43.3
31	▼ 1	Construction	46.5	47.1
32	–	Industrial Equipment	46.3	44.9
33	▼ 2	Consumer Durables	45.7	45.7
34	▲ 2	Life Sciences	45.5	41.6
35	▼ 1	Mining	43.5	43.1
36	▼ 1	Technology-Hardware	41.5	41.7

Data from Q4's results represent a notable change from the prior quarter's vulnerability rankings, which was led by the Energy, Power and Utilities industries. The Utilities industry's Total Vulnerability Score increased from Q3, while both Power and Energy fell. These two industries have likely seen the benefit of the economic recovery and the rotation of into cyclical stocks.

Transportation experienced the largest move up the ranking during the quarter, climbing 12 spots to 16th, likely a result of continued limitations to domestic and international travel as a result of the COVID-19 pandemic. Interestingly, the Restaurant industry moved the farthest down in the ranking during the quarter, falling 11 spots to 21st, likely a result of the relaxation of dining restrictions.

FTI Observations and Insights

Energy, Power & Products

Winds of change have been freshening in the energy sector over the last two quarters. Following several years of dismal performance relative to the broader U.S. equities markets, the group has been rallying. The most frequently cited explanations for the reversal are rising oil and gas prices, U.S. dollar weakness, investor rotation into "Value," and the anticipated post-pandemic surge in demand. Although those developments have provided meaningful tailwinds, there are more sector specific factors underpinning the revival, both of which have been in focus for activist investors: capital discipline and ESG.

The emergence of the U.S. unconventional paradigm has been one of the most disruptive technological advances in the history of the global energy industry. But the meteoric rise in production from shale producers was fueled by debt and serial outspending of cash flow from operations. After several years of fixating on production growth and contending with financial distress, the Exploration & Production industry is finally gravitating to a formula that aligns with what investors want: reinvest no more than 60-70% of operating cash flow back into the drill bit, pay down debt, and return excess capital to shareholders. This strategy provides an added benefit of constraining the light tight oil production growth that has proven so problematic on a global scale in recent years.

The second major development is the emergence of ESG and its transformational influence on the global energy landscape. Energy transition is no longer just a popular catch phrase – it is driving strategic pivots and capital allocation decisions. The international oil companies and largest energy services companies are reinventing their portfolios with unprecedented speed by investing in new energy technologies and embracing the commercial potential of decarbonization. Further down the market capitalization ladder, independent producers and services providers are also rethinking the way they operate by prioritizing emissions reductions, environmental stewardship and better alignment of corporate governance with the sector's capital providers.

This next phase of the energy sector's evolution will present its share of logistical, financial and strategic challenges. But the combination of sustained free cash flow generation and a willingness to embrace the energy transition has the potential to drive a renaissance for what had become a forgotten industry.

– Jeffrey Spittel, Senior Managing Director, Strategic Communications (Energy, Power and Products practice)

Health Solutions

Despite the COVID-19 pandemic, 2020 was a busy year for healthcare transactions with 128 deals, $198.2 billion in valuation. Deal activity was highest in the biotechnology sector (37 deals, $104.9 billion), pharmaceuticals (41 deals, $35.0 billion) and medical specialties (25 deals, $34.2 billion), followed by medical/nursing services (19 deals, $20.7 billion) and hospital/nursing management (5 deals, $2.3 billion).[30]

The average deal size was $1.6 billion, though driven by a few large deals > $10 billion: Astrazeneca-Alexion ($38.8 billion), Gilead Sciences-Immunomedics ($19.7 billion), Siemens-Varian Medical Systems ($16.2 billion) and Bristol Myers-Myocardia ($11.1 billion). Alexion, Immunomedics and Myocardia bring a portfolio of rare disease, breast cancer and solid tumor and cardiovascular drugs. Varian is the world leader in radiation oncology. In 2021, there will be 1.9 million new cases of cancer and 609 thousand deaths.[31] *Private equity was particularly busy in the medical/nursing services sector with several transactions > $1.0 billion focused on senior care (Clover Health, Cano Health, Help at Home). The managed care sector was limited to a single transaction: Centene's acquisition of Magellan Health focused on behavioral health ($2.4 billion).*[32]

Paradoxically, the COVID-19 pandemic has accelerated the digital transformation of healthcare, as exemplified by telehealth. Teladoc Health, the largest telehealth company has a market capitalization of $28.5 billion, followed by Amwell at $4.8 billion. Positioning for the future is ongoing with Teledoc purchasing Livongo for $18.5 billion, Google investing $100 million in Amwell, Cigna purchasing MDLive and most recently, Doctors on Demand merging with Grand Rounds. Telehealth is representative of the high level of interest in digital health exhibited by venture capital firms investing $9.7 billion in patient-centric, data-driven and potentially disruptive technologies.[33]

In summary, 2020 has been a year of transition for the healthcare services sector. Change is inevitable, but its magnitude, timing and direction remain unclear. However, certainty does exist regarding the non-sustainability of the projected two trillion dollar rise of healthcare spending to $6.2 trillion by 2028, 19.7% of the GDP.[34]

– David Gruber, Managing Director, Health Solutions practice

[30] FactSet; Proprietary research by FTI Consulting
[31] https://www.cancer.org/research/cancer-facts-statistics/all-cancer-facts-figures/cancer-facts-figures-2021.html
[32] FactSet; Proprietary research by FTI Consulting
[33] Pitchbook; Proprietary research by FTI Consulting
[34] https://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/NationalHealthExpendData/NationalHealthAccountsProjected

Special Purpose Acquisition Companies

The surge in SPACs in 2020 and 2021 has received enormous coverage. As of March 22, over 500 active SPACs today raised $233 billion through IPOs with 80% of them still searching for target companies. Of the 20% of SPACs that have agreed to acquire companies, their $36 billion of SPAC IPO funds acquired target companies aggregating $265 billion of enterprise value (including the use of other available financing, suggesting the remaining SPACs could acquire a trillion dollars of enterprise value companies over the next two years).[35] SPACs have followed the dramatic rebound in equity markets since March 2020 in the early days of the COVID-19 pandemic in the U.S. The result has been record trading levels for risk assets, such as high yield debt and equities, including SPACs particularly tech-driven stocks, which reached new highs in early 2021. The "SPAC Mafia" funded much of the 2020 SPAC boom, recycling funds through redemption or sale at de-SPAC merger date, holding the warrants. In 2021, investment banks and SPAC sponsors have sought more "long only" institutional investors. These broader trends, and SPACs' two-year lives, mean SPACs will not vanish any time soon even if the market cools.

SPACs and private investments in public equity ("PIPE ") financings represent ways for institutional and individual investors to buy these stories that would not have been available if companies were tapping into the venture capital, private equity or debt capital markets. The SPAC sponsor community is increasingly being represented by traditional private equity sponsors and some of the target companies being acquired by SPACs are portfolio companies of the private equity world. PIPEs historically filled a void in a CFO's repertoire to move quickly and quietly to finance during markets that are thinly traded or skittish for a "story" situation (April/May 2020). As 2020 wore on, the PIPE vehicle increasingly funded SPAC mergers. The valuation of SPAC mergers is driven by the availability and value affirmation by the PIPE market as PIPEs may represent a multiple of SPAC dollars. Any slowdown or pullback (as began in recent weeks) by the PIPE market could result in lower valuations for SPAC mergers. Target companies, inundated by unsolicited solicitations from SPACs, are prompting management teams and their investment bankers to run "SPAC-off" processes. The importance of PIPEs too is increasing their leverage over SPAC sponsors resulting in re-negotiated economics for the sponsors.

– Stuart Gleichenhaus, Senior Managing Director, Co-Leader of Merger Integration & Carve-outs

What This Means

The past year presented a once-in-a-century global pandemic, which upended many things, including both the broader capital markets and the universe of shareholder and corporate activists. While we do not expect 2021 to be a full return to normalcy, we do suspect that after a year of life in a pandemic, companies have adapted to the near-term challenges, settled into their updated business models and are once-again focused on the long-term strategy. We also suspect that investors, including traditional activists, long-only institutions and passive funds, share the same view and may be more likely to publicly voice their opinions toward under-performing companies. Given this viewpoint, we expect 2021 to continue with the fourth quarter's uptick in activism and provide a resurgence in activity, as a number of investors left a substantial amount of capital on the sidelines in 2020 and are likely ready to deploy it. While a number of the leading determinants of activist sentiment and activity in the coming year will be related to COVID-19, we expect the new Democratic administration to also be a factor in activity, specifically as related to an uptick in ESG-focused activism and shareholder proposals.

[35] https://spacalpha.com/

President Biden and the current Democratic Party have made it clear that climate change will be a key focus of the administration for the upcoming four years. One of President Biden's early moves was to nominate Gary Gensler, the former Chairman of the Commodity Futures Trading Commission, to lead the U.S. Securities and Exchange Commission ("SEC"). The Biden Administration and Mr. Gensler are expected to be more supportive on shareholder proposals related to environmental and social issues, whereas the Trump Administration largely advised the SEC to tether its support. Regarding his intentions as related to shareholder proposals, Mr. Gensler recently told members of the Senate Banking Committee, that "In 2021, there's tens of trillions of dollars of invested assets that are looking for more information about climate risk, and I think then the SEC has a role to play to help bring some consistency and comparability to those guidelines."[36] Many watch with interest to see what this means.

While the potential shareholder proposals will most directly impact the companies which receive them, they will also indirectly impact a growing field of sustainable investors and ESG-focused mutual funds. As the SEC takes a heightened interest in ESG and Climate Change shareholder proposals in 2021, and presumably for the duration of the Biden Administration, the voting patterns of ESG-oriented funds will also fall under the SEC's magnifying glass. All mutual fund managers and investment advisers are required to publicly disclose their proxy voting policies to current and potential investors. These proxy voting guideline and disclosure documents often fly under the radar of investors, but, per a recent SEC report, the individual policies are expected to come under increased scrutiny to determine whether investors are actually voting in accordance to their disclosed strategies.[37]

Despite the instability of the past year, or possibly because of it, corporate governance has come to the forefront of focus for both corporations and investors. No longer are corporate governance, specifically environmental, policies solely a focus for passive and long-only institutions, which have long publicized the importance of strong corporate governance policies. The past year saw the launch of multiple ESG and impact-focused activist investment firms and a number of highly publicized campaigns. With climate change set to remain a key initiative for the Biden Administration and the SEC, ESG is likely to remain a key focus for both corporations and investors alike.

FTI's Activism Vulnerability Screener Methodology

- The Activism Vulnerability Screener is a proprietary model that measures the vulnerability of public companies in the U.S. and Canada to shareholder activism by collecting criteria relevant to activist investors and benchmarking to sector peers.
- The criteria are sorted into four categories, scored on a scale of 0-25, (1) Governance, (2) Total Shareholder Return, (3) Balance Sheet and (4) Operating Performance, which are aggregated to a final Composite Vulnerability Score, scored on a scale of 0-100.
  - By classifying the relevant attributes and performance metrics into broader categories, FTI can quickly uncover where vulnerabilities are found, allowing for a more targeted response.

[36] https://www.wsj.com/articles/climate-change-emerges-as-a-compliance-focus-for-sec-11614802615?mod=article_inline
[37] https://www.wsj.com/articles/climate-change-emerges-as-a-compliance-focus-for-sec-11614802615?mod=article_inline

— FTI's Activism and M&A Solutions team determined these criteria through research of historical activist campaigns in order to locate themes and characteristics frequently targeted by activist investors. The following is a selection of themes that are included for each category:

Governance

— Proxy voting standard
— Board composition
— Proxy access

Total Shareholder Return

— Capital gains
— Dividend and share repurchase policy
— Relative valuation

Balance Sheet

— Capital allocation
— Leverage ratios
— Liquidity

Operating Performance

— Revenue and earnings growth
— Profitability margins
— Merger integration

— The Activism and M&A Solutions team closely follows the latest trends and developments in the world of shareholder activism. Due to the constantly evolving activism landscape, FTI consistently reviews the criteria and their respective weightings to ensure the utmost accuracy and efficacy of Activism Screener.

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