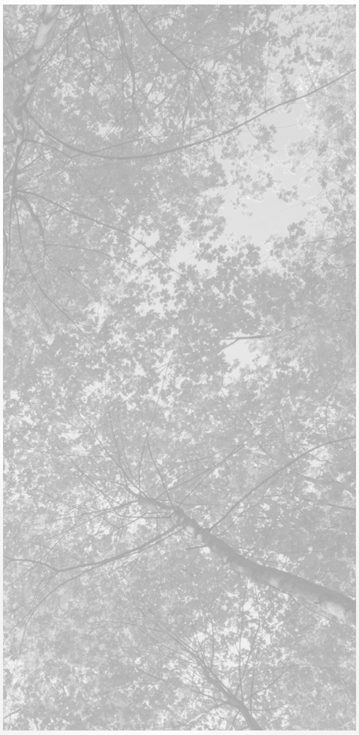
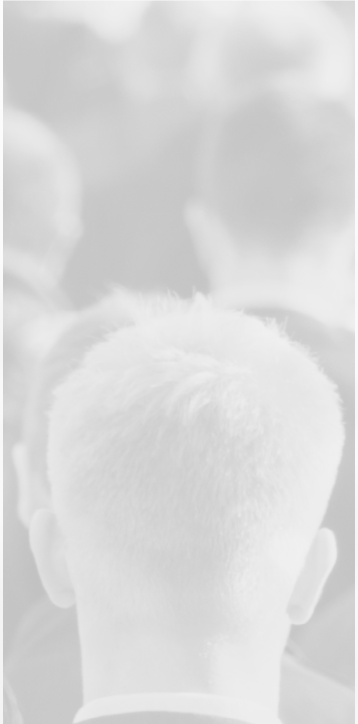


ESG ACTIVISM

2022

insightia
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CONTENTS

ESG Activism 2022

FOREWORD

Josh Black, Editor in Chief, Diligent

Josh Black
jblack@diligent.com

The second edition of our special report on ESG activism arrives in a surprisingly different environment to the first, even though just over a year has passed.

Last year, Engine No. 1 had just won three board seats at Exxon Mobil and shareholder support for environmental and social shareholder proposals was on the rise. It seemed inevitable that activist hedge funds would seek to tap this well of investor concern.

Indeed, they have. There was a sharp rise in ESG-themed proxy fights this year, and in other forms of ESG- and remuneration-led activism. But the success of these demands has been mixed.

Plenty of material to work with

It would be easy to dismiss the dip in support for ESG topics as a byproduct of rising energy prices and inflation. A tougher economic climate may sharpen the trade-offs required for meaningful ESG improvements, but investors are demanding greater disclosures and board changes in extreme cases, while also being more discerning.

As our report highlights, investors are looking at ESG with a fresh eye keenly focused on materiality. An instantly quotable verdict from BlackRock on climate proposals after the first wave of annual meetings perfectly captured the spirit of the year, warning that many of this year's "are more prescriptive or constraining on companies and may not promote long-term shareholder value." It said its support would drop as a result.

In order to do better next year, investors will need to make strong economic arguments.

As Jessica Strine of Sustainable Governance Partners points out in these pages, "ESG can't just be sprinkled on top of a campaign as an artificial additive."

Innisfree's Craig Pais makes the same point, telling Insightia, "if activists are to pursue successful ESG strategies, they will have to tie ESG issues to long-term shareholder value."

This year, Legion Partners Asset Management managed to make a compelling link between ESG and financial performance at Guess, although the fight was ultimately unwinnable, whereas Carl Icahn failed to do so with his argument about animal welfare – a peripheral issue even in the ESG world – at McDonald's and Kroger. At Huntsman, Starboard Value was arguing with a stock price that was already on the up.

No time to regress

Poor target selection by activists is just one reason directors should not be complacent about ESG in the coming year.

The introduction of the universal proxy card for U.S. contests is expected to increase nominations seeking to address ESG deficiencies, as well as from nontraditional activists. The Securities and Exchange Commission (SEC) has already passed a rule requiring greater disclosure of compensation metrics, including nonfinancial ones, and is expected to mandate broad environmental disclosures, including greenhouse gas (GHG) emissions from suppliers and customers in many cases. The EU's Corporate Sustainability Reporting Directive (CSRD) and Corporate Sustainability Due Diligence Directive (CSDDD) are expected to take effect from 2024 and 2025 but laggards could be called up sooner.

"Anytime there is a new regulation, a crop of shareholders will rise up, looking for companies to make foot fault errors, or even worse, to develop policies with which they subsequently fail to comply," Vinson & Elkins note in this report.

All the more reason for companies to consider an ESG materiality assessment – as explained herein by Diligent's Amanda Carty – and keep tabs on where investors are having the biggest impact with Insightia.

Thanks to Vinson & Elkins, Sustainable Governance Partners, and Innisfree M&A for contributing to this report, and to our colleagues at Manzama, whose news-tracking and visualization tools add a new element to this report.

THE GREEN RECKONING

With many green stocks underperforming their dirtiest peers, ESG activism faces more scrutiny and less support, writes Jason Booth.

After years of growth, ESG activism is suffering a crisis of confidence, beset by declining support, confusion about valuation, and a budding conservative backlash.

While the record number of ESG activist campaigns signals that the strategy is here to stay, boards of directors will need to be clearer about how their ESG initiatives benefit shareholders, while activist investors will need to be savvier about where they put their money.

A slew of full-time activists tried their hands at ESG activism this year. Few succeeded. Only 55% of global activist campaigns featuring both board representation and ESG-related demands had any success so far in 2022, down from 60% in 2021 and a 67% average for the entire 2018-2021 period.

The odds of winning were even smaller for activist campaigns combining only environmental and social (E&S) demands with board representation demands. In such cases, only one out of three campaigns saw partial success so far this year, down from five out of eight in 2021.

Elliott Management's recent campaign at Suncor ended with success, with the activist gaining a board seat and other concessions following a campaign highlighting, along with financial underperformance, employee safety issues. Voss Capital's campaign at Griffon Corp., which cited diversity and equality issues among its complaints, succeeded in gaining a seat on the board. Other ESG-flavored campaigns by the likes of Carl Icahn, Starboard Value, and Alta Fox Capital Management all went down in flames.

Dirty profits

Part of the problem creating confusion among ESG-savvy investors is the difficulty gauging the value of being a green company, especially at a time when dirty industry stocks like oil are booming.

A case in point is the 2021 investment by ESG-focused activist fund Inclusive Capital in Exxon Mobil, which has nearly doubled in value not because the company is cleaning up its act but due to the war in Ukraine and the lifting of COVID-19 travel restrictions boosting oil prices. By contrast, Inclusive's far cleaner investment in farm-products company Appharvest has lost roughly 75% of its value since the activist first disclosed its stake.

Such contradictions have increased skepticism on the part of proxy advisory firms, whose recommendations often determine the outcome of proxy votes. Glass Lewis' support for environmental and social proposals stood at just 37% at the end of the first half of 2022, down from around 59% on average throughout both 2021 and 2022. Institutional Shareholder Services (ISS) saw a smaller decline to 74% average support, down from 85% one year prior.

Anti-woke activism?

All this has helped set the stage for activists making proposals aimed at reversing ESG trends. Some U.S. states have threatened to place financial institutions on their restricted list for boycotting fossil fuels.

"Boards of directors will need to be clearer about how their ESG initiatives benefit shareholders, while activist investors will need to be savvier about where they put their money."

On August 4, the Attorney Generals of 19 U.S. states sent an open letter to BlackRock chief Larry Fink accusing the fund giant of using "the hard-earned money of our states' citizens to circumvent the best possible return on investment, as well as their vote." The National Center for Public Policy Research, meanwhile, has filed multiple "anti-woke" proposals arguing that ESG reporting is, in itself, discriminatory.

The reality is that activist investors will likely take a more focused approach, combining ESG with financial issues that resonate with shareholders more broadly. With stock prices down sharply this year, executive compensation is a likely target.

Glass Lewis, in particular, has raised concerns about management teams rewarding themselves based on ESG metrics that are hard to measure, writing, "we believe that shareholders should interrogate the use of metrics that award executives for ethical behavior or compliance with policies and regulation."

ESG activism isn't going away but the pace of its evolution means that it will occasionally outrun the appetite of institutional investors, especially when campaigns must be planned months in advance. No doubt activists are already learning from 2022 and preparing for next year.

ESG & remuneration activist campaigns by year and region

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022*
Asia	8	15	24	24	43	62	51	55	64	89
Australia	2	9	11	7	13	20	26	22	26	9
Canada	26	31	38	41	32	48	40	33	35	38
Europe	40	41	50	94	97	100	96	102	93	66
Other	8	11	12	8	16	15	10	6	15	1
U.S.	453	532	638	604	536	518	498	494	484	607

2013-2022* trend

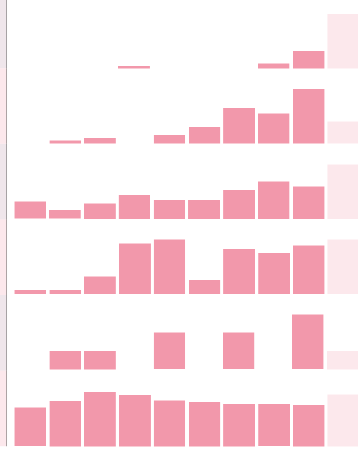
Number of activism campaigns inclusive of ESG and remuneration demands by company headquarter region and year.

*2022 data as of July 31
Source: Insightia | Activism

Environmental & social activist campaigns by year and region

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022*
Asia	-	-	-	1	-	-	-	2	7	22
Australia	-	1	2	-	3	6	13	11	20	8
Canada	10	5	9	14	11	11	17	22	19	32
Europe	2	2	9	26	28	7	23	21	25	28
Other	-	1	1	-	2	-	2	-	3	1
U.S.	162	219	208	231	231	174	179	180	168	310

2013-2022* trend



Number of activism campaigns inclusive of environmental and social demands by company headquarter region and year.

*2022 data as of July 31
Source: Insightia | Activism

ESG proxy fights in 2022

Elliott Management | **Suncor**

Activist gained a board seat and other concessions following a campaign highlighting employee safety as well as financial underperformance.

Legion Partners | **Guess**

Withhold campaign citing sexual harassment allegations won support from a majority of independent shareholders but not enough to force the resignation of company founders.

Carl Icahn | **McDonald's, Kroger**

Campaign highlighting mistreatment of pigs failed to win board seats, though the fast-food giant subsequently replaced two directors. Icahn withdrew similar Kroger demands following McDonald's defeat.

Voss Capital | **Griffon**

Activist gained one seat on the board of the fan maker following a campaign citing diversity and equality issues among its complaints.

Starboard Value | **Huntsman**

Jeff Smith's inclusion of climate change and emissions demands in this contest failed to garner any board seats at company's annual meeting.

Bluebell Partners | **Glencore**

Activist demands for Glencore to demerge its coal business and sell non-core assets failed to gain traction at the company's annual meeting.

Selected activist campaigns identified by Insightia reporters.

A RICH ENVIRONMENT FOR ESG ACTIVISM

An interview with Lawrence Elbaum and Patrick Gadson, co-heads, shareholder activism practice, and Margaret Peloso, lead sustainability partner, Vinson & Elkins.

Lawrence Elbaum
lelbaum@velaw.com

Patrick Gadson
pgadson@velaw.com

Margaret Peloso
mpeloso@velaw.com

How are activists in the U.S. adjusting their ESG campaigns?

Every single proxy season, activists find even more ways than in previous years to promote ESG themes in their proxy fights and other campaigns for corporate control. Of course, at the heart of each activism campaign is a thesis on unlocking corporate value for shareholders. However, activists know very well that the institutional shareholders – the electorate they need to win over in a proxy contest – are also increasingly focused on corporate hygiene, which includes championing growing lists of ESG initiatives. As a result, activists are including a growing number of demands for ESG reforms in their campaigns in order to win over shareholders and to punctuate their cases to unlock value.

Has ESG activism already peaked or is 2022 a deceptive lull?

ESG activism will never peak, unless institutional shareholders abandon these causes, which, in our view, is an impossibility. However, with COVID-19 headwinds fading somewhat in the rearview mirror, we expect that there will be an increase in campaigns targeting companies, and their boards, for significant drops in market value. We believe this will also lead to an uptick in activism focused principally on M&A. In the end, ESG activism will still be a significant force in these campaigns, but it may be masked by compelling economic campaign themes by activists.

What could the impact of the universal proxy be on the 2023 proxy season?

We expect the universal proxy to create a rich environment for first-time activists, particularly with small or ESG-focused funds, to seek minority board representation. This is because the new rules tend to make it easier from a cost perspective for these types of funds to run campaigns. And these activists will probably seek just one seat in most instances; trying to lean on companies to relent using an uncompelling "what's the harm in adding just one director?" argument.

Looking forward, do you expect the Securities and Exchange Commission's (SEC) proposed climate disclosure policy to impact ESG activism?

Yes. Anytime there is a new regulation, a crop of shareholders will rise up, looking for companies to make foot fault errors, or even worse, to develop policies with which they subsequently fail to comply. Additionally, the SEC's proposed rule has a number of areas where enhanced disclosure is required if a company has adopted particular risk management techniques or targets. These requirements are likely to shape the asks in climate shareholder proposals in 2023.

What is your biggest tip for issuers looking to protect themselves against an ESG-oriented activist campaign?

Well-prepared boards and their companies have a team of lawyers, investment bankers, boutique advisors, communication firms, and proxy solicitors in place long before a shareholder activist shows up. They are up to speed on the latest and greatest in terms of activism trends and defense techniques. They are closely monitoring and processing shareholder feedback, whether through routine quarterly engagements, annual meeting voting results, or proxy advisory firm recommendations and ESG scores.

Boards and companies with demonstrable track records of taking all this feedback seriously and, where appropriate, making proactive board, governance, and business changes, tend to be better situated for a successful defense when an ESG-oriented campaign arises.

GET AHEAD OF ESG RISK

ESG materiality assessments are the gold-standard in helping issuers understand their material ESG-related risks, writes Amanda Carty, general manager, ESG & data intelligence, Diligent.

Amanda Carty
acarty@diligent.com

In order to remain competitive in today's world, organizations across every sector know they must give as much thought to their environmental impact as they do their bottom line. This means actively working to develop sound sustainability policies and remaining transparent on issues such as water use and energy use.

With so many guidelines and regulations constantly evolving (and frequently overlapping), having a clear picture of your organization's most pressing ESG priorities is essential. To find that clarity and purpose, many businesses conduct an ESG materiality assessment, which helps to minimize uncertainty and ensure all efforts are focused where they're needed most. According to KPMG, 80% of Fortune 500 companies use ESG materiality in their reporting to identify risks, opportunities and trends.

What is an ESG materiality assessment?

An ESG materiality assessment is a process that allows businesses to evaluate the relative impact of ESG-related issues on their overall performance and viability. The process usually starts by clearly defining the scope and goals of the assessment, before deciding which internal and external stakeholders will be surveyed.

Then, those carrying out the assessment should create a list of potential issues to cover, before grouping and prioritizing those issues into a final shortlist. By categorizing the issues into a hierarchy, organizations can ensure a guided strategy that also offers a complete account of sustainability to investors. The shortlisted issues will be included in a survey for stakeholders, whose responses will help leaders prioritize their next steps.

It's worth noting that some ESG factors will only lead to a financial impact, while others will have a higher impact on stakeholders. It's important to consider both types of factors when reviewing the implications of ESG issues and strategies.

Why ESG materiality assessments matter

What can an ESG materiality assessment tell board directors? The answer is nearly everything they need to know to stay abreast of ESG trends, improve stakeholder engagement, and get ahead of potential risks.

The assessment highlights the issues that are most important to stakeholders, such as a company's impact on local communities or its sustainable supply chain practices, for prioritization. This also makes it easier to build a business case for investment in ESG projects, while helping businesses identify the areas of ESG that have the greatest impact on their performance and public perception.

But perhaps the most important benefit of a materiality assessment is the clear framework it provides for leaders to streamline their decision-making process when it comes to critical issues related to ESG. It allows directors to weigh the risks and benefits of taking certain actions, while also helping them to set clear priorities despite the complex nature of various competing interests.

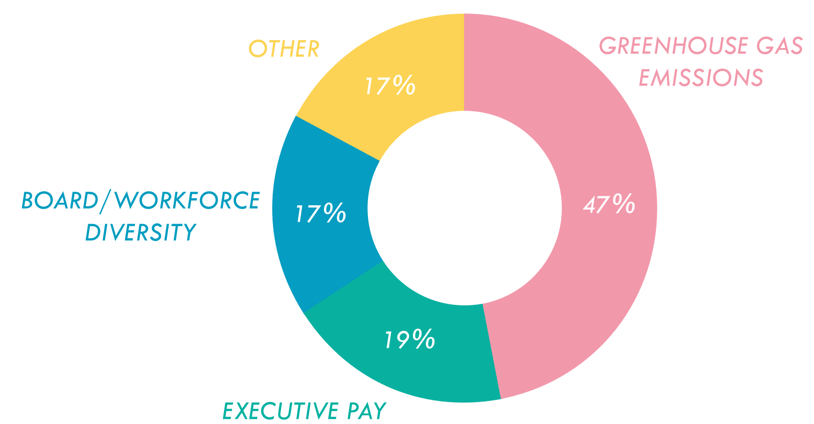
Improving ESG performance

Conducting a materiality assessment is an essential first step toward understanding your company's ESG programs and policies. Based on that understanding, you can create a baseline for measuring your ESG performance and also identify opportunities for improvement.

But because ESG best practices are ever-evolving, there's always more to learn. Continuing your education with resources like Diligent's **Climate Leadership Certificate Program** will arm you with the knowledge you need to manage climate risk and create sustainable growth strategies, so your organization can stay competitive while also meeting stakeholder expectations.

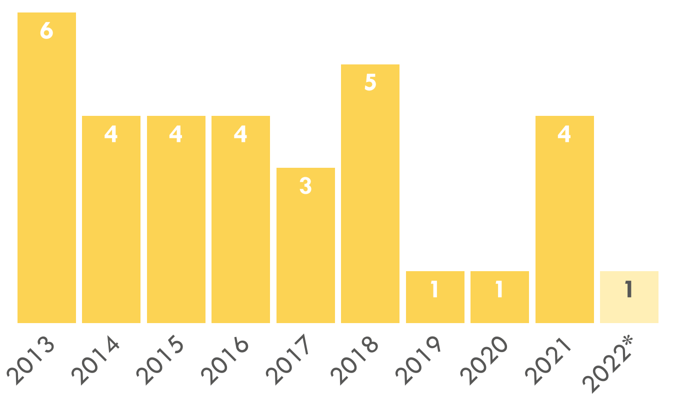
ESG ACTIVISM IN NUMBERS

What do you think is the biggest ESG issue right now?



Results of a poll presented to Insightia newsletter readers held on July 26, 2022.

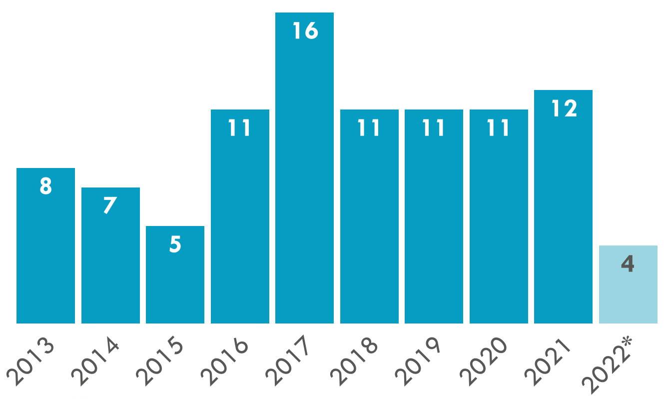
ESG activism in Canada



Number of activism campaigns inclusive of ESG demands launched by primary- and partial-focused activists at Canada-based companies, by year.

*2022 data as of July 31
Source: Insightia | Activism

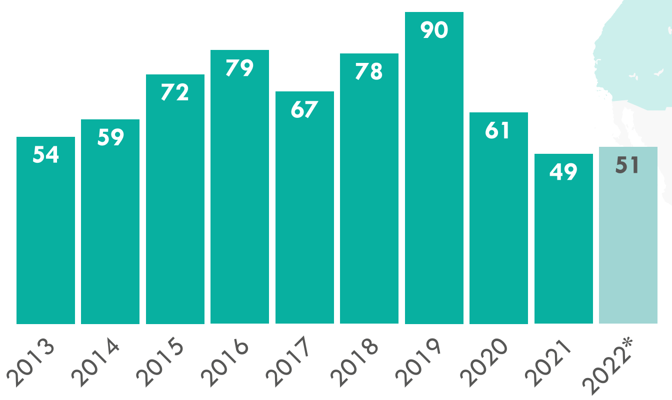
ESG activism in Europe



Number of activism campaigns inclusive of ESG demands launched by primary- and partial-focused activists at Europe-based companies, by year.

*2022 data as of July 31
Source: Insightia | Activism

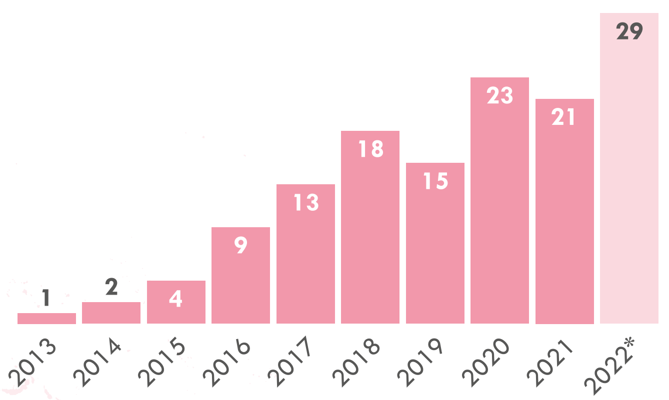
ESG activism in the U.S.



Number of activism campaigns inclusive of ESG demands launched by primary- and partial-focused activists at U.S.-based companies, by year.

*2022 data as of July 31
Source: Insightia | Activism

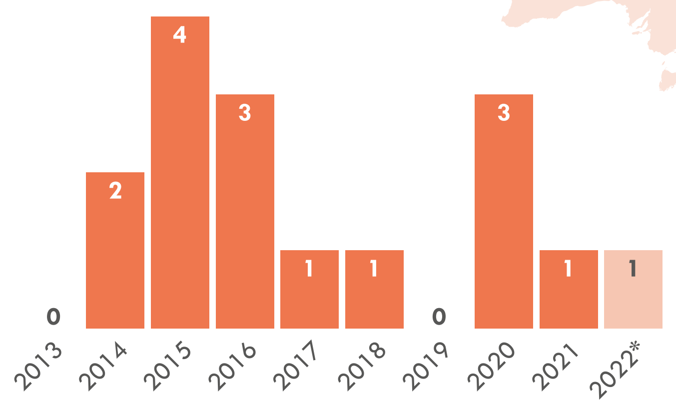
ESG activism in Asia



Number of activism campaigns inclusive of ESG demands launched by primary- and partial-focused activists at Asia-based companies, by year.

*2022 data as of July 31
Source: Insightia | Activism

ESG activism in Australia



Number of activism campaigns inclusive of ESG demands launched by primary- and partial-focused activists at Australia-based companies, by year.

*2022 data as of July 31
Source: Insightia | Activism

Top ESG activist investors in 2022

Top primary- and partial-focused activist investors by number of activist campaigns inclusive of environmental and social demands launched in 2022*.

*As of July 31,2022
Source: Insightia | Activism

DEMONSTRATING ESG LEADERSHIP

An interview with Jessica Strine, CEO, and Amy Hernandez Slowik, partner and associate director of research, Sustainable Governance Partners (SGP).

Jessica Strine
jessica.strine@sgpgovernance.com

Amy Hernandez Slowik
amy.hernandez@sgpgovernance.com

How are activists adjusting their ESG campaigns?

Jessica Strine (JS): While last year's Exxon vs Engine No. 1 battle put a spotlight on the role that ESG can play in an activist situation, its prominence and the climate angle embedded within the campaign, have perhaps sent some mixed signals to the market. Neither the Exxon campaign, nor many others, have been exclusively premised on ESG matters. Traditional drivers of activism still remain essential levers in a fight. And where ESG issues factor into a campaign, it begins and ends with issues that impact the bottom line, including the strength of individual directors and a company's exposure to long-term sustainability risks. ESG can't just be sprinkled on top of a campaign as an artificial additive in order to curry favor with the passive investors and the proxy advisors. It has to be grounded in materiality.

How might the universal proxy impact the 2023 proxy season?

Amy Hernandez Slowik (AS): We think you'll see some of the leading ESG activists put forth their own nominees, testing their effectiveness in areas where there is a combination of (a) poor oversight of a specific issue, and (b) the absence of board expertise on said issue. While it may be challenging for activists to put up nominees that can compete with most incumbent board directors, we do think that it sets up an interesting dynamic. We expect investors to deeply scrutinize board composition and how each individual director's skills and qualifications relate to the business.

Do you expect other sectors beyond energy to bear the brunt of ESG activist campaigns, going forward?

JS: Climate has become a universal issue and the focus has shifted from specific sectors toward instances where oversight is seen as lacking. An interesting example is Costco, where a proposal seeking Scope 3 emissions reporting won 69.9% support, despite the retailer not directly producing or refining hydrocarbons. This broader focus on emissions reflects the fact that climate change is expected to have real impacts on stocks, bonds, economies, and markets. As such, it is incumbent on every industry to play a role in addressing this systemic issue.

How have ESG shareholder proposals evolved this proxy season?

AS: We saw a trend of declining support for environmental and social (E&S) proposals in 2022, but digging into the proposals further shows a more nuanced story. This year, a significant number of proposals were settled to avoid potentially adverse voting outcomes, and many of the proposals that went to a vote were far more aggressive and prescriptive than in years past. Investors were not changing their views outright; it was the mix and volume of proposals, primarily, that changed.

Having said this, we do think that investors are applying more scrutiny, not taking a blanket approach toward E&S issues. They're digging into whether the issue is material and carefully evaluating whether a company's policies, oversight practices, and management of an issue are appropriate. This is a good thing as companies have more of an opportunity to demonstrate ESG leadership; however, they also cannot be complacent, as we expect that many proposals in 2023 will be more carefully crafted to appeal to investors.

JS: Some social issues have also taken on new prominence, in particular, racial equity. Many investors are seeing this issue as financially material, premised on the understanding that a company's reputation, brand, attractiveness to employees and customers, and/or dealings with regulators can be impacted by its handling of risks and opportunities related to social justice. We think this will be an area of focus for many investors over the coming years, and recommend companies prepare for off-season engagements on this topic.

CLIMATE ACTIVISM GETS PICKY

Environmental activist campaigns have soared to record numbers this season, but demand is dropping as investors get more climate-savvy, writes Miles Rogerson.

Activists have readily embraced environmental considerations in their campaigns this season, looking to replicate the success of Engine No. 1 at Exxon Mobil the previous year.

As of July 31, 2022, activists have made 132 campaigns inclusive of environmental public demands at U.S.- and European-headquartered companies this year, over double the 61 demands launched throughout 2021, according to Insightia's *Activism* module.

As was the case last season, the majority of successful environmental activist campaigns targeted the oil & gas sector, pushing the industry to curb its emissions and establish robust decarbonization strategies. But this year also borne witness to a growing number of environmental campaigns in the basic materials and real estate sectors.

Unlike last season, however, shareholder support for environmental proposals is falling, rather than rising. Only 15 (9.5%) of resolved campaigns have been successful, down from 18 (18.0%) campaigns in 2021.

Peer pressure

When Russia began its assault on Ukraine on February 24, activist investors were quick to respond, calling on companies from all sectors and industries to "cease all ties" with Russian oil, gas, and coal companies.

While BP, Shell, Equinor, and Exxon Mobil swiftly withdrew their Russian operations, TotalEnergies drew attention for failing to take swift action. In March, Clearway Capital warned the French energy giant to cease all operations in Russia or face a reckoning at its fast-approaching annual meeting.

Institutional investors soon joined the cause, with a group of 75 investors pushing TotalEnergies, Fortum/Uniper, and Wintershall DEA to suspend all Russia-based operations. TotalEnergies soon bowed to investor pressure and committed to stopping buying Russian oil and petroleum products by the end of the year.

On May 9, Third Point CEO Daniel Loeb also turned his sights back on Shell, reaffirming his belief that the U.K. oil giant should split its liquefied natural gas and renewables business from its carbon-intensive legacy energy business. The campaign, which began in October, has marked something of a turning point as activists focus on hiving off high emissions businesses, rather than the Engine No. 1 argument in favor of pouring oil profits into renewables.

Bluebell Capital has since followed suit, calling for Glencore to separate its coal business to help attract more environmentally conscious investors. Overseas, activist fund Enkraft submitted a proposal asking RWE to spin off its brown coal division, claiming such activities are detrimental to company value.

"If you separate the fossil fuel assets from the clean assets, then nothing fundamentally changes for the environment. The assets will be surviving, just in a new order," Giuseppe Bivona, partner and co-founder of Bluebell Capital Partners, told Insightia in an interview. "A good way to push energy companies to agree to the transition is to keep making sure that they have separated the future from the past."

"Activists have readily embraced environmental considerations in their campaigns this season, looking to replicate the success of Engine No. 1 at Exxon Mobil the previous year."

Always learning

Despite some environmental campaigns bearing fruit, many outside of the oil & gas sector have not experienced the same success. Land & Buildings' push for American Homes 4 Rent to strengthen its use of solar energy and Starboard Value's call for Huntsman Corp. to strengthen its climate governance are just two examples of environmental campaigns that failed to win the favor of investors. Bivona told Insightia that the decline in support for environmental campaigns boils down to a higher degree of knowledge on the subject matter among institutional investors.

"Generally, investors are moving from a place of blank approval to these climate requests, to an environment which is more selective and offers a higher degree of knowledge that enables them to make a much more informed decision," he said. "As such, the level of scrutiny and attention is higher and therefore investors are more selective in which issue they support."

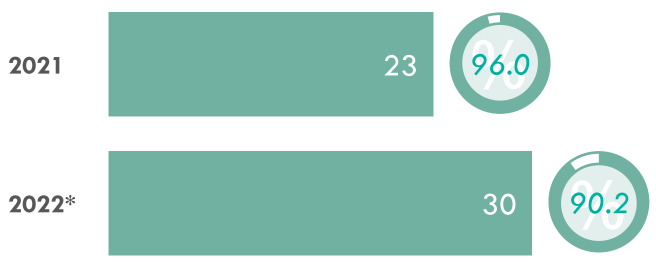
Environmental shareholder proposals at U.S. companies by sector and year

	2017		2018		2019		2020		2021		2022*		2017-2022*	
	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)
Basic materials	2	19.7	1	7.8	2	6.9	-	-	2	61.1	-	-	7	26.1
Communication services	3	20.1	-	-	1	28.2	-	-	1	39.0	2	21.8	7	24.4
Consumer cyclical	11	18.5	6	25.6	7	33.5	4	27.6	6	48.7	10	40.8	44	32.2
Consumer defensive	13	21.8	9	26.9	7	17.9	7	37.2	7	37.9	9	42.8	52	30.0
Energy	18	37.0	9	45.0	6	24.2	6	35.2	8	53.6	13	38.7	60	40.1
Financial services	7	9.2	5	24.8	-	-	2	32.0	2	22.6	13	16.6	29	18.0
Healthcare	3	25.8	3	32.8	-	-	-	-	-	-	-	-	6	28.1
Industrials	8	28.4	12	33.3	7	28.7	9	32.0	8	54.2	8	42.0	52	36.7
Real estate	-	-	1	31.1	-	-	-	-	-	-	-	-	1	31.1
Technology	-	-	2	29.3	1	9.7	3	25.8	3	12.2	3	19.8	12	21.7
Utilities	16	39.1	10	19.3	5	18.1	2	5.5	6	8.4	5	33.6	44	31.1

Number and average support for environmental-related shareholder proposals at U.S.-based companies by sector and year.

*2022 data as of July 31
Source: Insightia | Voting

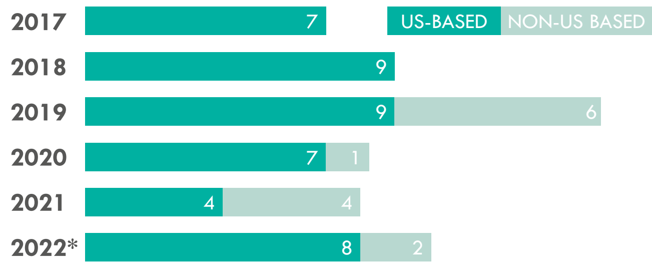
Slow march of "say on climate" votes



Number and average support for (%) management "say on climate" proposals.

*2022 data as of July 31
Source: Insightia | Voting

Activist climate change campaigns



Number of activist campaigns inclusive of climate change and GHG emissions demands launched by primary- and partial-focused activists by company HQ and year.

*2022 data as of July 31
Source: Insightia | Activism

DIVERSITY MATTERS

As predicted in last year's ESG Activism report, social matters have become increasingly important to investors, writes Rebecca Sherratt.

Historically, activists have rarely made social considerations major components of their campaigns but this changed in 2022. Diversity and human rights formed part of several high-profile campaigns and won support from institutional investors.

The number of campaigns inclusive of social demands made at companies globally skyrocketed to 236 as of July 31 this year, compared to 168 and 157 demands throughout the whole of 2020 and 2021, respectively, according to Insightia's *Activism* module.

As has also been the case with social proposals filed by institutional investors, activist demands of this type were primarily concentrated in the U.S., a consequence of the 2020 Black Lives Matter protests highlighting racial inequity in the country.

Diversity and equality demands were especially common this season, with LivePerson, American Vanguard, and Rocky Mountain Chocolate Factory all facing pressure to enhance board diversity to unlock shareholder value.

Taking up the mantle

Legion Partners' proxy fight at Guess demonstrated how ESG shortcomings can significantly impact financial value, the activist pushing for the removal of co-founders Paul and Maurice Marciano amid allegations of sexual misconduct and a decade of stock underperformance. Sure enough, in 2021 Guess' stock took a further 45% plunge after a flurry of related lawsuits.

"The activist's success in raising those issues [sexual harassment allegations] goes to the heart of the personality and effectiveness of management," Charles Elson, founding director of the Weinberg Center for Corporate Governance, told Insightia in an interview. "It crosses into the legal, which is why I think those issues will be more successful than those that are purely political."

Current labor shortages have also exacerbated human capital concerns, Amy Borrus of the Council of Institutional Investors (CII) told Insightia that a company under the pall of sexual misconduct could "lose out on finding the best and the brightest when companies are competing for talent."

Legion ultimately failed to remove the Marciano brothers at Guess' April 22 shareholder meeting, but 84% of independent shareholders voted against the Marciano brothers' reelection. Following the vote, the brothers bought additional shares, securing their position still further.

Expanding the investor toolkit

Despite an overall lull in support for ESG shareholder proposals, social proposals experienced a surge in filings and the topic of racial equity dominated investor engagement in the 2022 proxy season.

Diversity audit proposals more than tripled from the previous year. In total, 22 diversity audits, seeking third-party assessments of how a company's policies and practices address racial and civil rights, were subject to a vote at U.S.-listed companies in the first half of the year, eight of which won majority support.

"Social proposals experienced a surge in filings and the topic of racial equity dominated investor engagement in the 2022 proxy season."

Issuers quickly took note, many reaching withdrawal agreements to conduct audits, including companies such as Amazon and Tyson Foods, which have been historically resistant toward investor engagement.

Adrienne Monley, managing director at PJT Camberview, told Insightia in an interview that the success of diversity audits this year, despite the broader decline in support for ESG proposals, "reflects investors' focus in diversity, equity, and inclusion (DEI) – a topic that has garnered more interest over the course of the pandemic."

Diversity audits also won the favor of leading investors. BlackRock and JP Morgan voted in favor of eight of the nine diversity audits subject to a vote in 2021, according to Insightia's *Voting* module.

"While these proposals have received significant investor and market attention, only a handful of companies have conducted and publicly disclosed their audit to date," Monley said. "Expect investors to focus on the quality and substance of these disclosures once available, as well as to expand the number of companies they target next year."

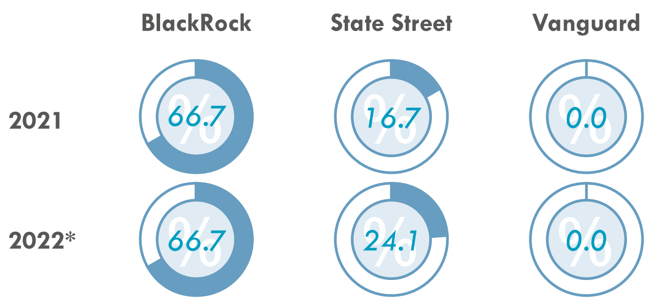
Social shareholder proposals at U.S. companies by sector and year

	2017		2018		2019		2020		2021		2022*		2017-2022*	
	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)	No. proposals	Average support (%)
Basic materials	4	30.8	2	20.7	2	38.4	-	-	1	83.8	-	-	9	36.1
Communication services	5	27.8	5	26.1	4	32.5	5	25.8	5	44.3	13	24.6	37	28.9
Consumer cyclical	19	18.3	17	26.7	27	27.8	28	29.0	24	35.1	37	25.1	152	27.2
Consumer defensive	18	11.4	8	20.6	9	24.3	12	22.1	14	20.4	26	17.9	87	18.4
Energy	9	22.1	5	25.2	3	31.9	4	28.4	3	44.7	4	26.6	28	27.7
Financial services	18	21.2	18	25.4	13	26.0	10	23.9	14	34.6	17	20.2	90	24.9
Funds	9	0.0	-	-	-	-	2	0.0	-	-	-	-	11	0.0
Healthcare	9	19.9	12	24.4	9	34.1	14	36.2	12	39.5	33	26.4	89	29.5
Industrials	19	17.9	13	32.5	18	30.7	23	36.7	18	40.7	23	32.8	114	32.0
Real estate	1	84.8	-	-	10	32.3	2	39.7	1	66.3	-	-	14	39.6
Technology	22	18.6	16	19.5	16	20.8	13	27.5	19	35.6	31	24.2	117	24.3
Utilities	10	28.4	9	32.4	9	40.6	6	36.6	4	23.6	4	25.6	42	32.3

Number and average support for environmental-related shareholder proposals at U.S.-based companies by sector and year.

*2022 data as of July 31
Source: Insightia | Voting

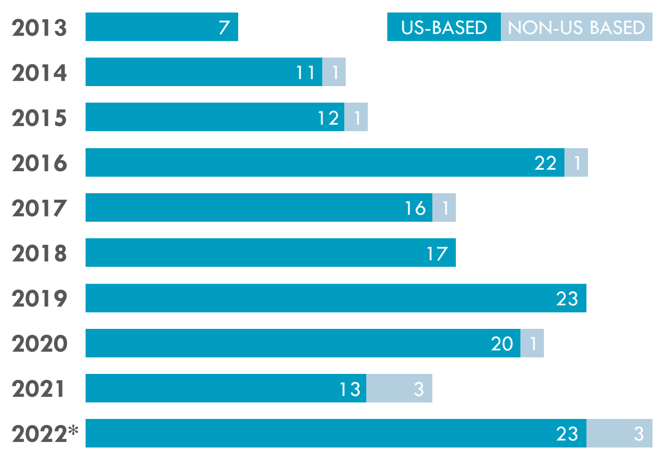
Support for diversity audits



Average support by investor for (%) racial equity audits at U.S.-based companies by year.

*2022 data as of July 31
Source: Insightia | Voting

Social activist campaigns



Number of activist campaigns inclusive of social demands launched by primary- and partial-focused activists by company HQ and year.

*2022 data as of July 31
Source: Insightia | Activism

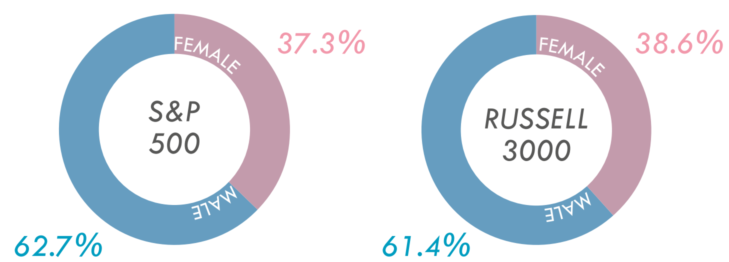
Ethnicity* of S&P500 directors by gender

	No.		%	
	Male	Female	Male	Female
American Indian/Alaskan native	-	2	-	0.5
Asian	45	23	4.8	5.4
Black or African American	118	73	12.5	17.0
Hispanic/Latin	51	17	5.4	4.0
Mixed	9	8	1.0	1.9
Other	4	-	0.4	-
Pacific Islander	1	1	0.1	0.2
White	717	305	75.9	71.1

Ethnicity breakdown of directors at S&P500 companies by gender. *Where disclosed.

Data as of July 31, 2022
Source: Insightia | Governance

Director appointments by gender in 2022



Proportion of new director appointments at companies in the S&P 500 and Russell 3000 in 2022* by gender.

*Data as of July 31, 2022
Source: Insightia | Governance

ENHANCED ESG SCRUTINY

An interview with Gabrielle Wolf, director, and Craig Pais, investor engagement manager, Innisfree.

Gabrielle Wolf
gwolf@innisfreema.com

Craig Pais
cpais@innisfreema.com

Innisfree®

Do retail investors care about ESG?

GW: With the rise of retail investing, some public companies are contending with larger proportions of retail investors. Unlike institutional investors, individual retail holders are more apathetic, and only 20% of such holders generally vote. With the rise of commission-free investing and easy-to-use apps, one would think we would witness a shift in how such retail holders vote.

The common belief is that millennials care about climate change and racial injustice and will use their shareholdings to push companies to address these issues. Proxy voting data does not support this assertion. Institutional investors are far more likely than retail investors to support shareholder proposals calling for more rigorous ESG oversight. Even under the heightened glare of media-heavy proxy contests including Huntsman, Guess, McDonald's, and Exxon Mobil, retail continued to favor management in the face of dissident campaigns driven by ESG concerns. Until millennials are willing to put their votes where their mouths are, it will be up to institutional investors to press companies to make progress on ESG goals for which millennials loudly advocate but do not actually defend.

For institutional investors, how important are ESG issues in proxy contests?

CP: The most notable ESG-focused campaign this proxy season was at McDonald's, where Carl Icahn pressed the company to end its use of gestation crates for pregnant pigs in its supply chain.

The major proxy advisory firms and large index funds were not convinced this was a compelling argument for change. Institutional Shareholder Services (ISS) indicated it could not support an ESG-centric campaign when Icahn (with his tiny position of 200 shares in the company) would be financially disconnected from the impact of his proposals on McDonald's financial performance. Glass Lewis noted Icahn had taken a "simplistic and myopic view of ESG concerns" with limited consideration for the creation of shareholder value. McDonald's went on to secure a decisive victory over Icahn.

Clearly, if activists are to pursue successful ESG strategies, they will have to tie ESG issues to long-term shareholder value.

What are investors' priorities around human capital management proposals?

GW: Institutional investors' human capital management priorities continue to shift to reflect the sentiments of the public and asset holders. During the height of COVID-19 and following the murder of George Floyd, investor focus pivoted from customer satisfaction to employee safety and diversity, equity, and inclusion efforts.

In 2022, as rising inflation forewarned of a recession and the Russian invasion of Ukraine increased market volatility, investors retreated from supporting ESG proposals. Index funds' decreased support indicates their deferential approach that will not second guess a board's determination if the board demonstrates that it is informed and actively overseeing material ESG risks. As a recession looms, it remains to be seen whether ESG factors will continue to garner widespread investor support – or if asset managers will refocus on purely financial metrics.

What's on the ESG horizon?

CP: We see two key developments on the horizon. The SEC's proposed rule for climate-related disclosure will bring significant changes. Assuming the final rules are effective by the end of this year, large accelerated filers would be required to provide these new disclosures in 2024 for fiscal year 2023.

The ESG rating industry is also subject to enhanced scrutiny. Pressure has grown in both the U.S. and Europe for consistent ESG ratings data and regulation of ESG ratings providers themselves. Currently, without consistent and comparable ESG disclosures, there is a significant variance in ratings between providers, and it is often unclear which factors these providers even consider. As the demand for ESG investing grows, so too will the demand for reliable ESG data.

Innisfree M&A provides issuers with strategic advice on ESG matters, including shareholder engagement, corporate communications, and shareholder impact, overseeing shareholder outreach to develop a customized ESG engagement program. Our experience and relationships developed through participation in most major proxy contests and M&A transactions provide Innisfree an unparalleled understanding of institutional investors, retail campaigns, proxy advisory firms, and ESG disclosure frameworks.

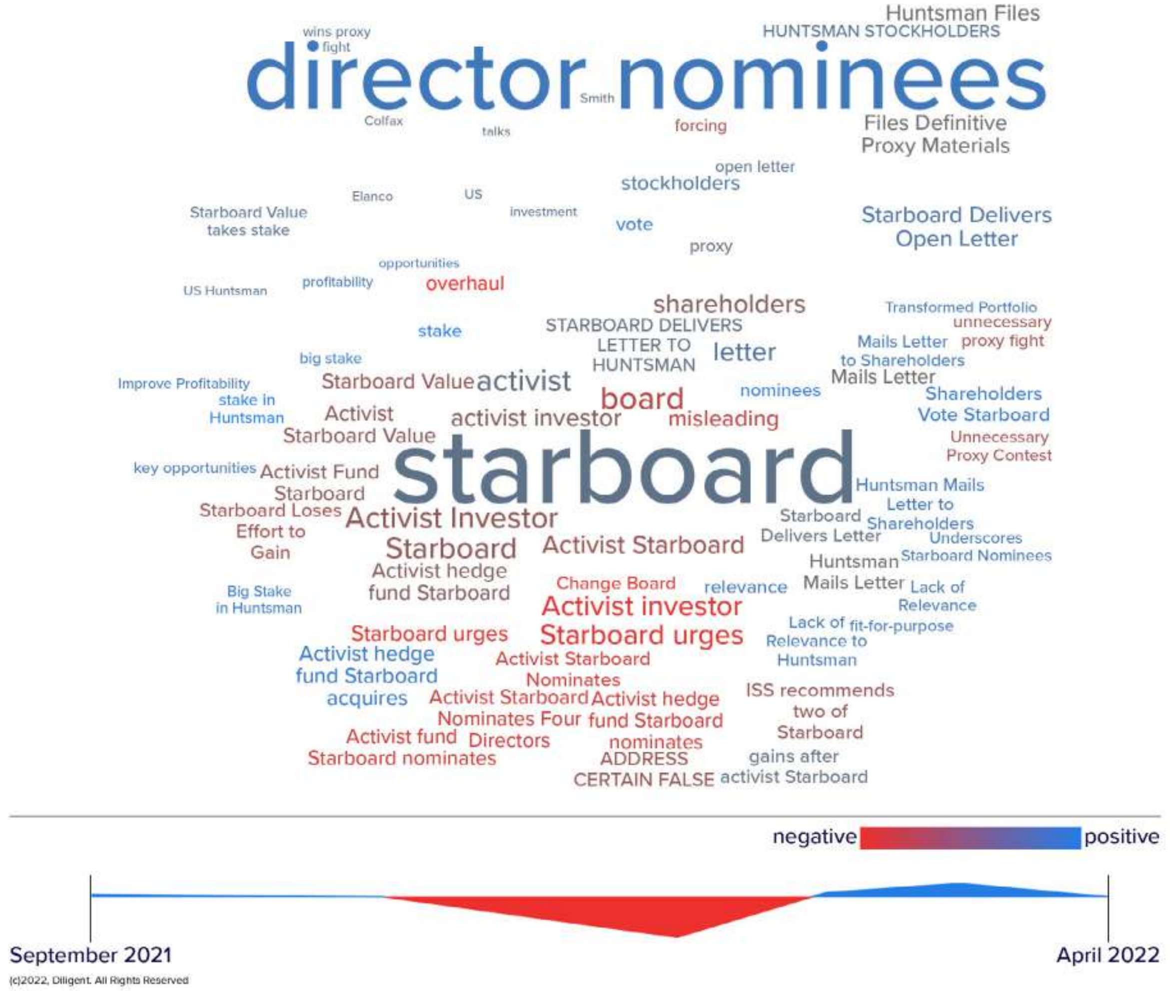
ESG IN THE NEWS

The following charts, taken from Diligent's content analysis and monitoring software Manzama, reveal the top news terms associated with various companies subject to activist engagement in the recent proxy season, filtered by shareholder news.

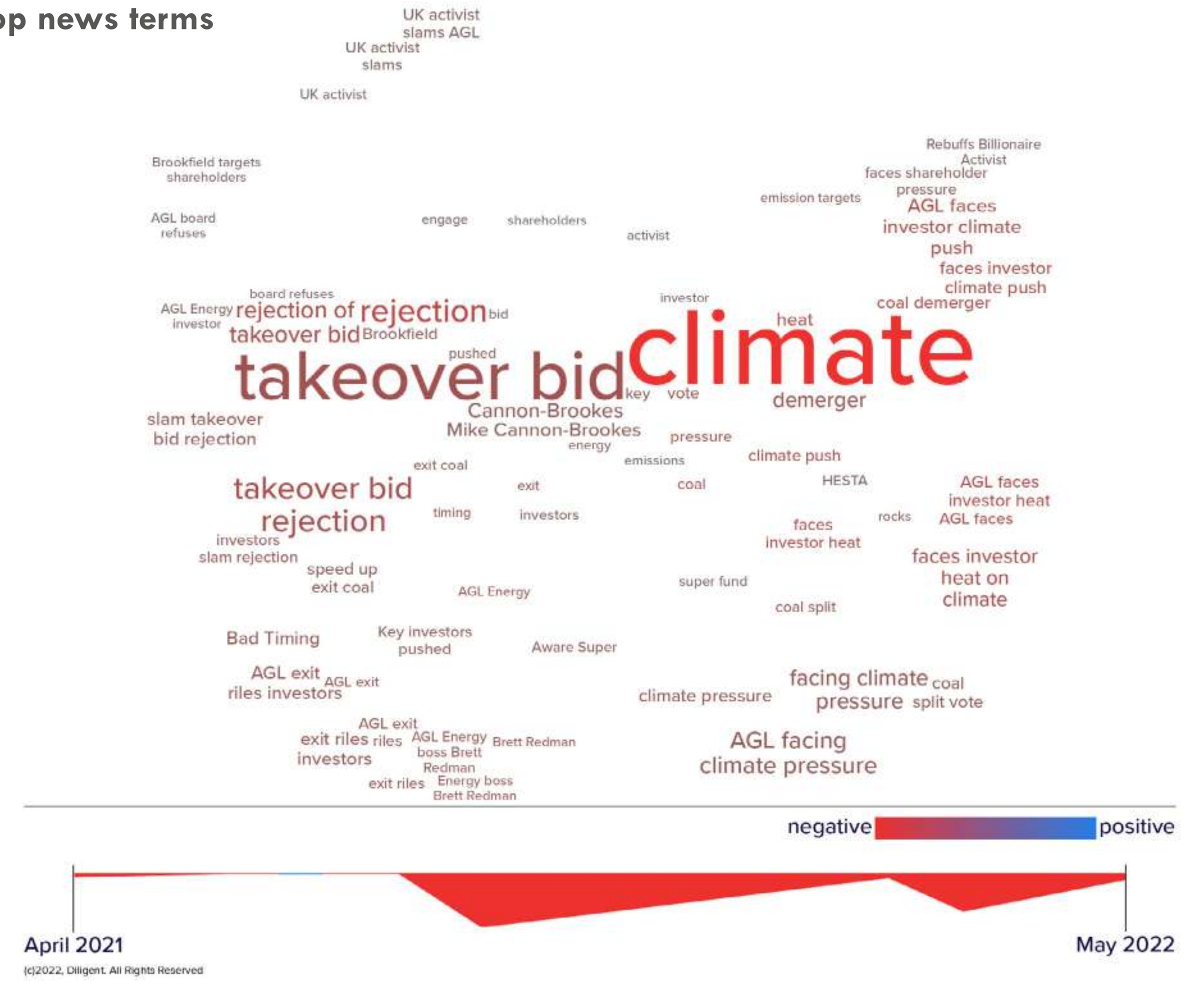
KEY: Frequent news terms > Less frequent news terms

Positive connotations — Negative connotations

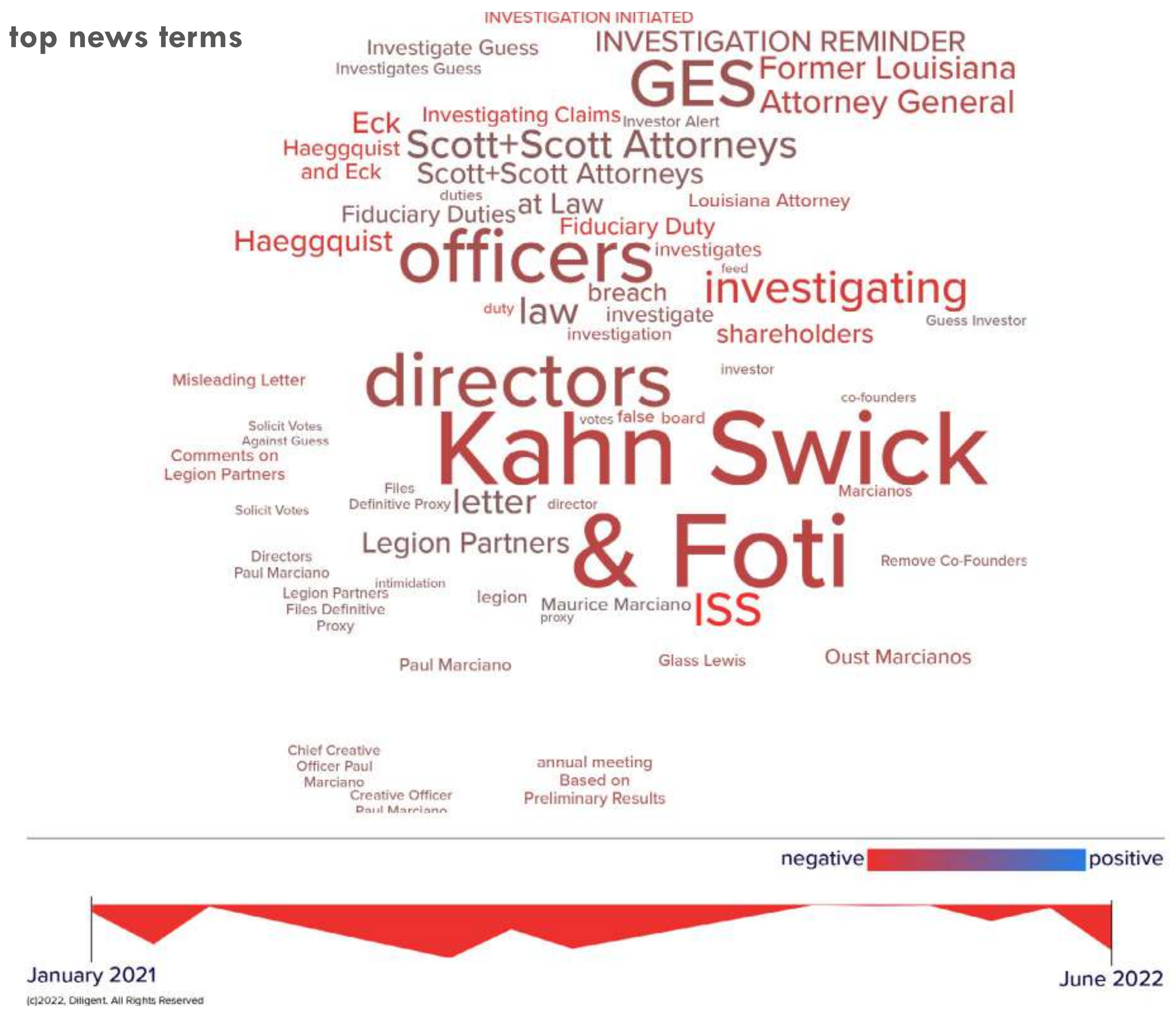
Huntsman top news terms



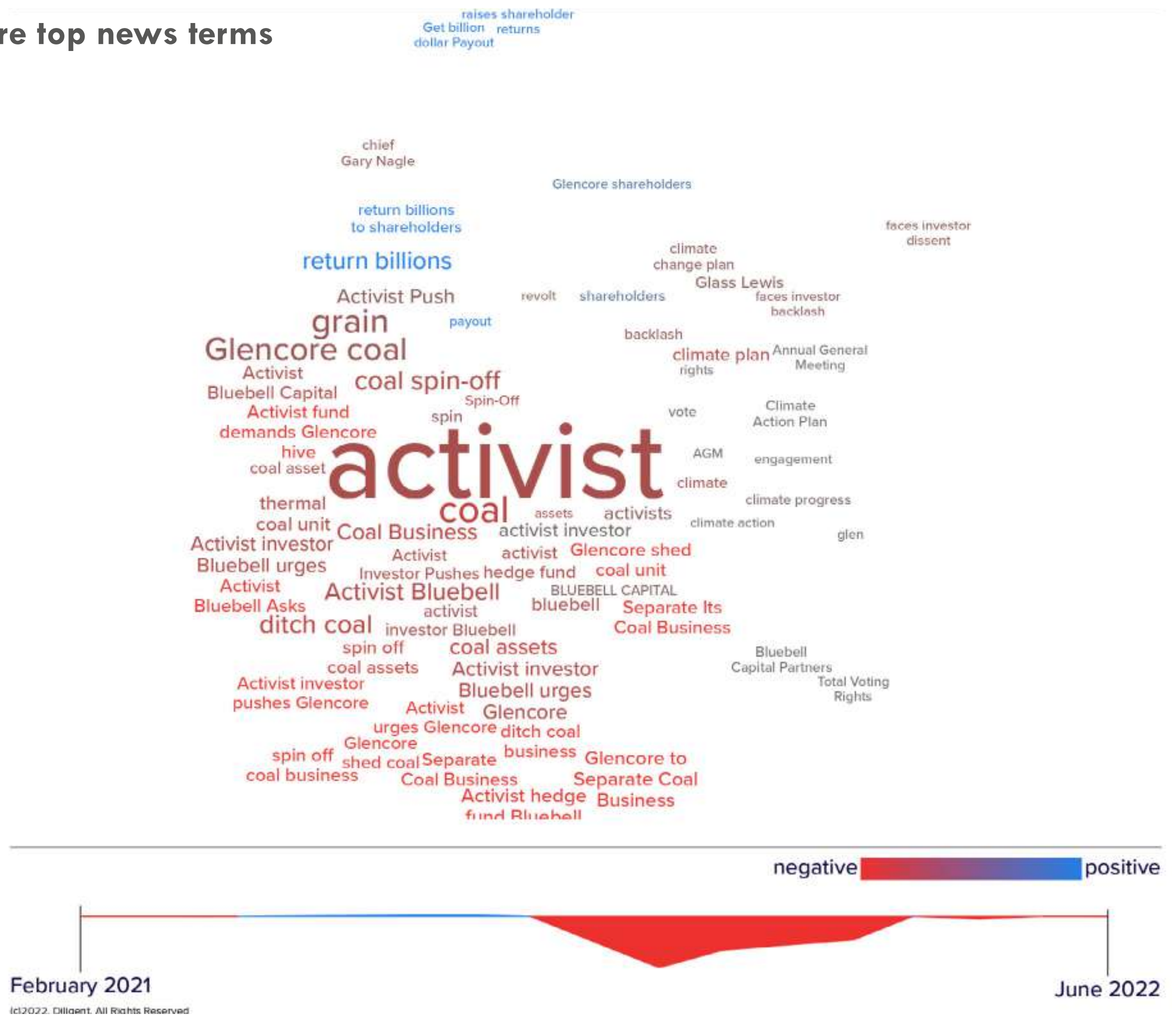
AGL top news terms



Guess top news terms



Glencore top news terms



McDonald's top news terms