

## Module 3

### The Role of Global Capital Markets

Market Discipline  
(To keep companies honest)

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## Holding management to account...

A forum to transact company business where shareholders have an opportunity to ask questions of, and make comments on, the company's Board of Directors, management and auditor.

Management and Board presentation of:

- Annual financial report
- Director's report
- Auditor's report
- Auditor's appointment and remuneration.





## What happens at AGMs?

Shareholders can ask **questions...**

Chair of an AGM must allow a reasonable opportunity for the shareholders to ask questions about or make comments on the management of the company... but there is no obligation to answer!

**Resolutions and motions...**

Shareholders with at least 5% of the votes, or at least 100 shareholders entitled to vote can notify the company in writing of a proposed resolution.

Passing requires 51% of all votes.

*Difficult?* Yes, with institutional investors and proxy votes...

## If management doesn't listen...

### **Two strikes policy**

Hold directors accountable for executive compensation.

Strike 1:

- A no-vote of  $\geq 25\%$  on remuneration report at AGM.

Strike 2:

- Subsequent remuneration report also receives a no-vote of  $\geq 25\%$ .
- At that second AGM, shareholders will vote to determine whether all directors will need to stand for re-election (a spill) – requires  $> 50\%$  vote.

*Still difficult?*

## A takeover threat

Final resort is to vote with your feet: SELL.  
With sufficient support, this will cause price pressure.

If the price drops below “intrinsic” value, the shares will look cheap to predators:

- Competitors
- Private equity
- Corporate raiders.

## Shareholder activism

Using share ownership to put public pressure on company management for:

- Financial gain
- Environmental concerns
- Social concerns
- Governance concerns.

Focus on:

- Divestment of loss-making divisions
- Excessive executive compensation
- Irresponsible/unsustainable investment
- ‘Sin’ divestment (tobacco, carbon, ...)
- Employee welfare
- Unethical overseas business practices
- Board directorships.





## Shareholder activism

From a bad 1980s reputation of corporate raiders using *Leveraged Buy Outs* to a 2010s reputation of *agents for (corporate) change*.

- AGM resolutions
- Share proxy battles require substantial ownership stakes
- PR/media campaigns
- Dialogue with management are possible with relatively small stakes.

Institutional investors play an important role (e.g. CalPERS).

## Do debt markets discipline corporations?

Superficially, no!

Debt holders are not owners who can hold management to account.

Corporations participate mostly in the primary debt markets, but...

- Buy-back debt on the secondary market
- Periodically refinance existing debt
- Issue new debt for new investment projects
- Violating bond covenants may cause technical default and lead to a downgraded rating
- Yield changes may signal bad news to shareholders.

## Source list

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