Deep Dive: Activist Hedge Funds

- Educational Presentation #17 – Activist Hedge Funds
- 6. Feb. 2026
- Property of the ESCP Alternative Investments Society
- Sources: Bloomberg, Skadden, Company Websites, Barclays IB, Candor, WallStreetPrep, Technical University of Darmstadt, Investopedia

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Section I: Introduction and Overview

Overview of Activist Hedge Funds

- Activist hedge funds acquire significant stakes in public companies where they believe shareholder value is constrained by governance or strategic inefficiencies
- The goal is to unlock value by actively influencing management decisions
- Returns depend on the successful execution of the activist campaign rather than passive participation in equity markets

Activist Investing ≠ Traditional Equity Investing or Private Equity

Activist Investing	Traditional Equity Investing	Private Equity
Large minority equity stakes, typically ~5–10%	Small minority equity positions, typically below 1–2%	Majority or full equity ownership
Active engagement with corporate leadership to drive change	Passive ownership with no direct influence over corporate decisions	Full operational and strategic control
Returns driven by strategic, operational, financial or governance changes resulting from intervention	Returns driven by earnings growth, dividends and changes in market valuation	Returns driven by operational improvements, leverage effects and exit multiple expansion
Medium-term investment horizon, usually 1–3 years	Variable, often long-term	Long-term investment horizon, usually 3–7 years

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Why Activist Hedge Funds Work

The Agency Problem

- Managers are expected to maximize shareholder value, but their personal incentives often differ from those of shareholders -> conflict of interest
- Management may prioritize compensation, job security or reputation over long-term value creation
- Fragmented ownership and insufficient board oversight limit effective monitoring and accountability of management decisions

Consequences

- **Capital misallocation:** Investment decisions prioritize risk avoidance over return on invested capital
- **Excess cash retention:** Cash is held on the balance sheet or deployed into low-return uses instead of being distributed to shareholders
- **Delayed portfolio optimization:** Underperforming assets or business units are kept for too long due to resistance to divestment or restructuring
- **Rising operating inefficiency:** Weakened accountability leads to increased operating costs and structural complexity

Key takeaway:
Management does not always act in the way that maximizes shareholder value due to limited accountability and misaligned personal incentives. Activist hedge funds address this agency problem by increasing oversight and pressure on management to encourage decisions that are better aligned with shareholder interests and long-term value creation.

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Section II: Different Types of Activist Hedge Funds

Operational Activism

Definition

- **Objective:** Targeting fundamental “under-management” to drive margin expansion and bridge the valuation gap between the target and its best-in-class peers
- **Tactics:** Benchmarking KPIs against competitors, forcing headcount rationalization, optimizing supply chains, installing industry veterans on the board to oversee a turnaround

Operational activists benchmark key metrics such as EBITDA margin, SG&A, and ROIC against best-in-class peers to quantify underperformance. The performance gap underpins the turnaround thesis, often combined with incentive realignment to tie compensation to capital efficiency rather than revenue growth.

Main players

STARBOARD VALUE

- **Founder:** Jeffery Smith, Mark Mitchell
- **Founded:** 2002
- **Strategy:** Proxy fights, board refresh
- **Annual Returns:** 15.5% (2023)
- **AUM:** $9bn (2025)

Cevian Capital

- **Founder:** Christer Gardell
- **Founded:** 2000
- **Strategy:** Concentrated stakes, constructive engagement
- **Annual Returns:** 17.67% (2025)
- **AUM:** $14bn (2025)

Structural Activism

Definition

- **Objective:** Addressing the conglomerate discount of an organization where the market fails to value a company's individual business units in their current bundling
- **Tactics:** Aggressive push for spin-off or carve-out of non-core assets, optimizing the capital structure through debt recapitalization, and facilitating divestures or take-private transactions

Structural activism often relies on a sum-of-the-parts valuation, where business units are valued separately using industry multiples. The gap between implied standalone value and market valuation represents the conglomerate discount the activist aims to unlock.

Main players

ELLIOTT

- **Founder:** Paul Singer
- **Founded:** 1977
- **Strategy:** Value gap analysis, push for divestment
- **Annual Returns:** 14.2% (2023)
- **AUM:** $73bn (2025)

TCI Fund Management

- **Founder:** Chris Hohn
- **Founded:** 2003
- **Strategy:** Value gap analysis, push for divestment
- **Annual Returns:** 27.8% (2025)
- **AUM:** $77bn (2025)

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Governance Activism (ESG)

Definition

- **Objective:** Protecting the Terminal Value of the target company by forcing the management to account for long-term tail risks, ranging from climate litigation to poor board oversight. This is the most widespread type of activism
- **Tactics:** Launching Proxy contests to replace stale directors, eliminating dual-class share structures to open decision-making power, demanding verified disclosures on sustainability and executive compensation agreements

Proxy contests require SEC filings and shareholder vote solicitation, often influenced by proxy advisors such as ISS and Glass Lewis. Full proxy fights can cost $20m+, making them credible but expensive. Since 2022, shareholders can mix board candidates from both slates on one ballot.

Main players



- **Founder:** Christopher James
- **Founded:** 2020
- **Strategy:** Active ownership and engagement
- **Annual Returns:** N/A
- **AUM:** $300m (2025)



- **Founder:** Jeffrey Ubben
- **Founded:** 2000
- **Strategy:** Collaborative work with management/boards
- **Annual Returns:** 39% (2023)
- **AUM:** $11bn (2025)

Short Activism

Definition

- **Objective:** Correcting market overvaluation by exposing fundamental flaws, fraud or unethical business practices in the target company, acting as a market policeman deflating asset bubbles
- **Tactics:** Publication of ”short reports” and taking significant short positions to profit from an anticipated price drop, initiating legal proceedings against a target company

Short activists conduct forensic research before building a short position and publishing their findings. Risk is asymmetric, with unlimited theoretical losses and exposure to squeezes and litigation. The EU requires disclosure above 0.5%, while the US has no equivalent rule.

Main players

MUDDY WATERS RESEARCH

- **Founder:** Carson Block
- **Founded:** 2010
- **Strategy:** Identification of accounting fraud
- **Annual Returns:** ≈19% (2023)
- **AUM:** $308m (2025)

HINDENBURG RESEARCH

- **Founder:** Nate Anderson
- **Founded:** 2017
- **Strategy:** Whistle-blower analysis, forensic investigations
- **Annual Returns:** N/A
- **AUM:** $640m (2024)

Section III: Structure of an Activist Campaign

Target Identification

Activist campaigns begin with identifying companies where structural weaknesses and misaligned incentives create a path to value creation



Structural Vulnerability

- Agency problems and weak governance
- Conglomerate or complex structure
- Suboptimal capital allocation



Valuation Dislocation

- Persistent discount to peers or intrinsic value
- Clear sum-of-the-parts upside
- Assets undervalued due to inertia, not fundamentals



Feasibility of Influence

- Ownership base fragmented
- Board refresh cycles or weak shareholder alignment
- Realistic path to influence without full control



Catalyst Visibility

- Identifiable actions that unlock value
- Change within a finite time horizon
- No reliance on macro or multiple expansion



Hard Constraints

- Regulatory or political barriers
- Strategic shareholders or dual-class structures
- Liquidity sufficient for meaningful stake

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Economic Model of an Activist Campaign

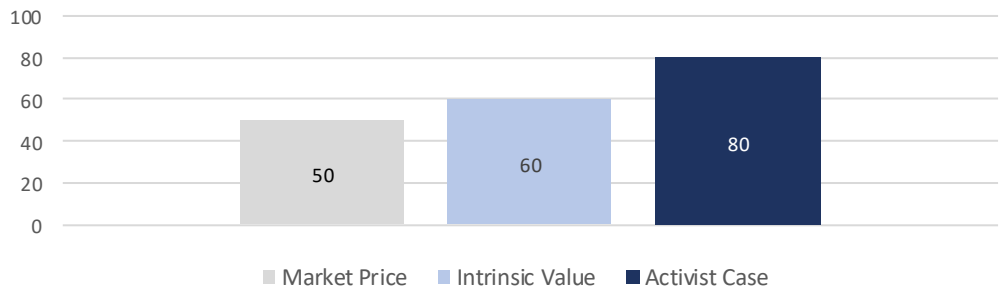
Activism is underwritten as a probability-weighted value unlock over time

Entry Economics

Entry Price vs Intrinsic Value

Activist looks at:
- Current market price
- Standalone intrinsic value
- Activist value case

Example case (simplified):



Gives the activist investor:
- Margin of safety without intervention (10)
- Additional upside from change (30)

Value Creation Levers

Operational Improve-ments	• Cost cuts • Margin normalization • Revenue refocus
Capital Allocation Changes	• Excess cash distribution • Share buybacks • Deleveraging or recap
Strategic Actions	• Spin-off • Asset sale • Sale of the entire company
Multiple Re-Rating	• Reduction of conglomerate discount • Governance premium

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Position Construction and Disclosure Strategy

Stake building in activist investing is a tactical process shaped by disclosure rules, market liquidity, and control considerations

Stake Building Strategy

Target Ownership
- Typical stake: 3–10%
- Large enough to be credible
- Small enough to avoid control obligations

Liquidity constraints
- Average daily volume caps accumulation speed
- Building 5% in an illiquid name can take months

Market impact
- Aggressive buying raises entry price
- Stealth accumulation preserves economics

Disclosure Mechanics (U.S. Example)

5% threshold
- Crossing 5% triggers disclosure
- Filing required within 10 days

13D vs 13G
- 13D → Active intent, can influence control
- 13G → Passive investor, no activist intent

Strategic trade-off
- File early → Signal seriousness
- Accumulate first → Better economics

Instrument Choice and Economic Exposure

Cash equity
- Voting power
- Direct ownership credibility
- Most common structure

Derivatives (e.g. swaps)
- Economic exposure without immediate voting rights
- Can delay disclosure in some jurisdictions
- Counterparty and regulatory risk

Leverage
- Rarely excessive
- Activism relies more on influence than leverage

Capital at Risk and Portfolio Construction

Concentration
- Often top 3 positions
- 5–15% of fund capital

Time horizon
- Often 12–36 months
- Capital effectively locked

Reputation capital
- Public activism affects future campaigns
- Credibility matters

Opportunity cost
- Capital tied in slow campaigns reduces portfolio turnover

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Section IV: Limitations & Risk

Why Activism Is High-Conviction and High-Risk

Time Horizon & Capital Lock-Up

- Activist campaigns typically require 12–36 months to play out
- Capital is effectively locked while outcomes depend on board response and shareholder votes
- Limited liquidity compared with traditional long-only equity strategies



Extended timelines convert valuation risk into execution and governance risk

Why Activism Is High-Conviction

- **Clear agency problem**: Dispersed ownership and weak monitoring create opportunities for value-enhancing intervention
- **Identifiable, actionable catalysts**: Board changes, capital allocation shifts, asset sales, or strategic alternatives
- **Empirical support**: Activist engagement is associated with positive abnormal returns on average, despite wide dispersion

Why Risk Is Structurally Elevated

- **Minority ownership model**: Activists intentionally operate without control
- **Binary, path-dependent outcomes**: Success depends on execution, not valuation alone
- **External dependencies**: Outcomes influenced by markets, regulation, and third-party voters

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Management Entrenchment & Defensive Measures

Structural Defences

- **Poison pills / rights plans:** Dilute activist ownership and deter stake accumulation, increasing cost and reducing influence
- **Dual-class share structures:** Concentrate voting power with insiders, weakening shareholder democracy and limiting activist leverage
- **Staggered boards & governance provisions:** Delay board turnover and slow the pace of strategic change

Collective Action Problems

- **Coalition risk:** Activists typically hold **~1–10% stakes**, requiring support from other shareholders to win votes
- **Fragmented shareholder base:** Split incentives across institutions make coordination difficult
- **Free-rider problem:** Activists bear engagement and proxy costs, while passive shareholders benefit without active support

Escalation of Governance Resistance



As governance defences escalate from structural barriers to outright confrontation, the probability of a successful activist outcome declines while time, cost, and uncertainty increase

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Market, Macro & Sector Risk: Energy & Utilities

Energy and utilities illustrate how macro shocks translate into valuation compression, refinancing stress, and strategic vulnerability

Market / Macro Shock

Interest rates remain elevated:

- UK Bank Rate ~**3.75%**
- ECB policy rate ~**2.0–2.15%**
- **Energy price volatility:** European natural gas prices recently hit a 10-month high (≈€42.60/MWh) due to low storage and supply pressure

Sector Impact

In energy & utilities, which are inherently asset-heavy:

- **Lower equity valuations** as discount rates rise
- **Stressed balance sheets** from refinancing at higher rates
- **Less flexibility** on capex and dividends

Why Activists Step In

Activist investors push for:

- **Capital allocation changes** (dividends vs debt payoff or reinvestment)
- **Asset divestments / spin-offs**
- **Board & governance changes**

Mispriced risk + inefficient strategy exposed by macro shock

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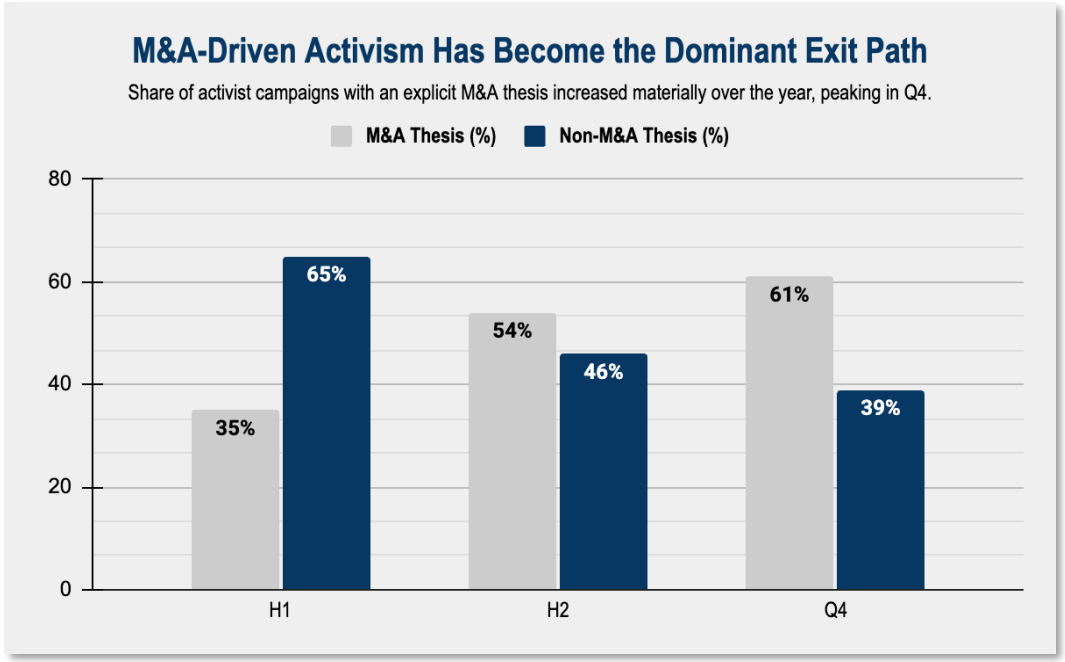
Market & Capital Market Risk

Market Environment Matters

- Robust M&A activity, elevated equity volatility, and constructive financing conditions supported a record 255 activist campaigns globally
- Market conditions materially influence both the feasibility and timing of activist exits

Activist Theses Are Increasingly M&A-Dependent

- **Exit feasibility is market-dependent:** widening credit spreads reduce buyer financing capacity and transaction certainty
- **Private equity bids weaken** as leverage becomes more expensive, reducing strategic alternatives
- **Regulatory intervention** can delay or block transactions, extending holding periods
- **Sector concentration amplifies risk:** activist campaigns cluster in Industrials, Technology, and Healthcare
- **Correlated sector downturns** lead to synchronized drawdowns across activist portfolios



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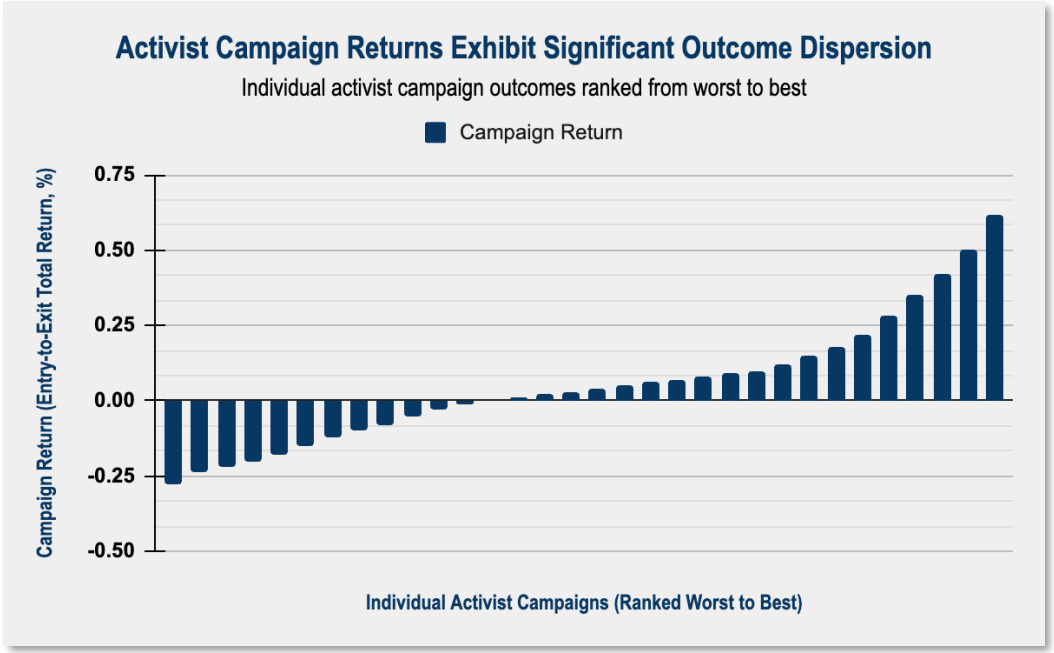
Asymmetric Payoffs & Outcome Dispersion

Evidence from Prior Research

- **Activist returns are highly dispersed**: A small number of campaigns generate a disproportionate share of total value, while many deliver modest or negative outcomes
- **Early alpha is not persistent**: Aggressive activists may outperform initially, but return advantages fade post-announcement in multiple studies
- **Announcement pops are short-lived**: Targets can experience ~5% abnormal returns within ~16 trading days, which do not reliably translate into long-term excess returns

Implications for Risk-Adjusted Performance

- **Headline IRRs are misleading** when volatility, drawdowns, and tail risk are ignored
- **Activism must be assessed as a portfolio strategy, using:**
- **Sharpe** (total volatility)
- **Sortino** (downside risk)
- **Treynor** (market beta exposure)



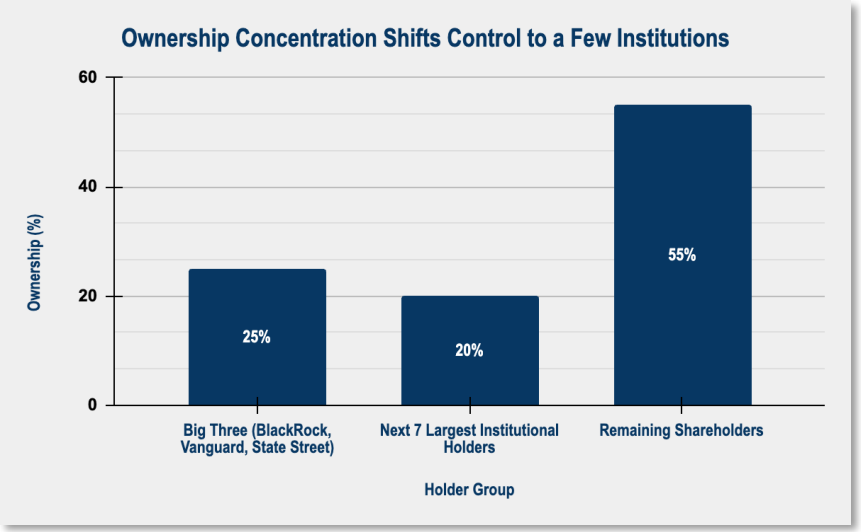
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Regulatory & Ecosystem Risks:

Why control and outcomes depend on rules, not just ownership

Ownership Concentration Limits Activist Control

- Activist positions are economically meaningful but structurally non-controlling (~1–10%)
- Top 10 holders control ~45% of shares at large-cap U.S. companies; Big Three control ~25%
- Outcomes are institution-driven, not ownership-driven



Regulation Shifts Execution Risk & Expected Returns

- Accelerated disclosure (13D / 13G modernization) compresses activists' stealth window, raising entry prices and reducing optionality
- Universal proxy mechanics increase shareholder choice but introduce vote-splitting risk, raising dispersion in contested outcomes
- Institutional voters operate under fiduciary and regulatory constraints, expanding the influence of governance norms and proxy advisors over pure return maximization

Ownership ≠ control
Control ≠ economic logic
Control = votes × rules

Activist investing is as much about navigating a regulated voting ecosystem as identifying undervalued assets

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Section V: Case Studies

Structural Activism – Case Study

Elliott and AT&T

Involved Parties:

- **Name**: Elliott Investment Management
- **Founder**: Paul Singer
- **Founded**: 1977
- **Type**: Activist hedge fund

- **Name**: AT&T Inc.
- **Founder**: Alexander Graham Bell
- **Founded**: 1885
- **Type**: Telecommunications company

Position / Action / Results

- **Position:** Elliott quietly builds a minority equity stake in AT&T of approximately $3.2b in 2019
- **Action:** Aggressive public campaign pushing for asset divestments, deleveraging and strategic focus
- **Results:** Spin-off of media business through separation of WarnerMedia and DirecTV from AT&T's core telecom business, reducing conglomerate discount

The campaign of Elliott Management against AT&T is a clear example of structural activism. Elliott built a significant minority stake in stealth and launched a public campaign through a detailed letter criticizing AT&T's capital allocation and strategy. By maintaining pressure and signaling a credible threat of a proxy fight, Elliott pushed AT&T to engage, leading to strategic simplification, governance changes, and the eventual separation of WarnerMedia and DirecTV from AT&T's core telecom business. This led to a meaningful share price recovery during the campaign period and generated substantial returns for Elliott.

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Operational Activism – Case Study

Pershing Square and Canadian Pacific Railway

Involved Parties:

- **Name**: Pershing Square Holdings
- **Founder**: William A. Ackman
- **Founded**: 2004
- **Type**: Activist hedge fund

- **Name**: Canadian Pacific Railway
- **Founder**: George Stephen
- **Founded**: 1881
- **Type**: Railway transportation company

Position / Action / Results

- **Position:** Pershing Square builds a significant minority stake of approximately 14% in Canadian Pacific Railway in 2011
- **Action:** Aggressive campaign, including a proxy fight to replace CEO and board members, supported by detailed competitor benchmarking and an operational turnaround plan
- **Results:** Replacement of senior management with industry veterans, sharp improvements in operating efficiency and margins, major valuation re-rating

Pershing Square's campaign against Canadian Pacific shows how operational activism can unlock value. In 2011, Ackman invested $1.1b for a large minority stake and ran a proxy fight to replace the CEO and the board. The new CEO was rail veteran Hunter Harrison, and some of the new board members were Pershing Square employees. The following operational overhaul achieved substantial improvements in efficiency, profitability, and shareholder value. Pershing Square exited in 2016 with significant profits.

Governance Activism – Case Study

Engine No.1 and ExxonMobil

Involved Parties:

- **Name:** Engine No. 1
- **Founder:** Christopher James
- **Founded:** 2020
- **Type:** Activist hedge fund ("impact driven ownership")

- **Name**: ExxonMobil Corporation
- **Founder**: N/A (formed via merger of Exxon + Mobil)
- **Founded**: 1999
- **Type**: Integrated oil & gas major

Position / Action / Results

- **Position:** Engine No. 1 builds a relatively small Exxon stake (reported ~$40m in Dec 2020)
- **Action**: Launches a proxy contest (Dec 2020) and nominates 4 directors, arguing Exxon needs stronger board oversight, better capital allocation discipline, and credible long-term strategy
- **Results:** Shareholders elect 3 Engine No. 1 nominees to Exxon's board in 2021. Exxon also states it would reconsider shareholder proposals that won majority support on lobbying/climate reporting

Engine No. 1's campaign against ExxonMobil challenges the traditional axiom that "might makes right" in corporate governance, demonstrating that a strategic narrative can outweigh raw capital. With only a 0.02% stake, the fund bypassed the need for a controlling interest by treating passive index giants (BlackRock and Vanguard) as constituents to be won over. By reframing climate inaction as a fundamental failure of capital allocation rather than solely an environmental issue, they successfully mobilized institutional voters to replace three directors.

Short Activism – Case Study

Hindenburg Research and Nikola Motors

Involved Parties:

- **Name:** Hindenburg Research
- **Founder:** Nate Anderson
- **Founded:** 2017
- **Type:** Short-Only research firm

- **Name**: Nikola Motor Company
- **Founder**: Trevor Milton
- **Founded**: 2014
- **Type**: Battery-electric + hydrogen fuel-cell truck manufacturer

Position / Action / Results

- **Position:** Discloses a short position in Nikola (NKLA) ahead of publication (10 Sep 2020)
- **Action**: Publishes a forensic report alleging systemic misrepresentation (incl. the “Nikola One in Motion” video being staged)
- **Results:** Immediate sell-off; SEC begins examining the allegations 4 days after report publishing; Milton resigns (21 Sep 2020); later Nikola pays $125m to settle SEC charges (Dec 2021) and files Chapter 11 (Feb 2025)

Hindenburg Research's campaign against Nikola Motors demonstrates how activist hedge funds can assume a regulatory function in global equity markets. It was not the SEC or another official institution that uncovered Nikola's active investor fraud. Rather, it was Hindenburg Research's independent forensic investigation that identified key issues, including a video showing a "rolling" Nikola One truck having been recorded on a downhill road. This video identified the company as grossly overstating its technical developments. The activist report led to an SEC investigation, jail term for Trevor Milton and an eventual delisting of Nikola Motors.

Poison Pill – Case Study

Icahn and Netflix

Involved Parties:

- **Name**: Icahn Enterprises L.P.
- **Founder**: Carl C. Icahn
- **Founded**: 1987
- **Type**: Activist hedge fund

- **Name**: Netflix, Inc.
- **Founder**: Reed Hastings, Marc Randolph
- **Founded**: 1997
- **Type**: Entertainment company

Position / Action / Results

- **Position:** In 2012, Icahn acquires a meaningful minority stake of approximately $321m (~10%) in Netflix, signaling activist intentions and openly suggesting a sale of the company
- **Defensive Action:** Netflix adopts a poison pill, allowing existent shareholders to buy at a discount to prevent Icahn from increasing his stake beyond a threshold of 10%
- **Results:** Icahn does not increase his stake but still earns ~$2b on his investment; Netflix remains independent

Following his disclosure of a minority stake in Netflix, Icahn quickly escalated by publicly arguing that the company was a logical acquisition target and openly suggesting a sale. This triggered Netflix to adopt a poison pill that stopped Icahn from increasing his stake. Icahn later agreed to a standstill. The stock performed strongly, and Icahn exited with roughly $2b in gains. This case is a strong example of an effective poison pill: it was adopted within days of Icahn's disclosure, never triggered, acted purely as a deterrent and allowed Netflix to continue performing strongly.



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