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Protocol – Session 3
Active Owners and Firm Policies

Speaker: Vicente Cuñat
Discussant: Oğuzhan Karakaş

Vicente Cuñat is an Associate Professor at the Department of Finance of the London School of Economics. His research interests include topics in corporate governance, corporate finance and managerial economics such as mergers and acquisitions, corporate voting, financing constraints, trade credit, information provision and incentive contracts. He has published theoretical and empirical work in the American Economic Review, The Journal of Finance, the Journal of Financial Economics, the Review of Financial Studies and the Journal of the European Economic Association among others. He is a graduate of the Universidad de Valencia and holds an MSc from CEMFI. His PhD is from the department of Economics of the London School of Economics. He is a council member and honorary fellow of the Spanish Economic Association and has been awarded the young economist award by the EEA, the Jaime Fernandez de Araoz corporate finance price and the Brattle Group's Distinguished Paper Award.

Oğuzhan Karakaş is a University Senior Lecturer in Finance at the Cambridge Judge Business School (CJBS). He is also a Fellow of the Centre for Endowment Asset Management of CJBS, the Cambridge Endowment for Research in Finance of CJBS, and the J M Keynes Fellowship in Financial Economics. He received his PhD at London Business School. Oğuzhan's research focuses on Corporate Governance (particularly in Ownership and Control), Corporate Social Responsibility, Private Equity, and Dynamic Investment Strategies. His research has appeared in leading academic journals, including the Journal of Finance, Review of Financial Studies, and Journal of Financial Economics.

Protocol of Session 3, Friday 7 June (14.30 p.m. – 15.30 p.m.)

In the first part of the third session, a joint paper by Ruth Aguilera, Vicente Bermejo, Javier Capapé and Vicente Cuñat on "Active Owners and Firm Policies" is presented. The presentation starts with the distinction between two polar forms of influence: active and passive investors. The paper tries to contribute to the question whether active ownership investors can affect firm policies. Sovereign Wealth Funds constitute a specific class of active investors. These have specific preferences going beyond returns. The focus of the paper lies on firms' reactions to changes in investor preferences. More precisely, in November 2012, Norway's sovereign wealth fund (NBIM) unexpectedly announced a note that it would enhance corporate governance in its portfolio firms by articulating specific governance expectations. This sudden change in governance preferences is utilized as a natural experiment to understand shareholder influence among active ownership investors. The presenter introduces the empirical strategy of the paper: NBIM specific measure of governance reflecting NBIMs new preferences and a DiD-Approach is employed using the change in preferences. The overall effect of the announcement on the overall governance level of NBIM is positive. Furthermore, the overall effect is then decomposed into re-weighting, the change in governance as well as the cross product. Afterwards, the presenter discusses the change in NBIMs investment strategy after the announcement: Do firms that enter NBIM have better governance post-announcement? Yes; those which exit have worse corporate governance. In short, NBIM investment strategy aligns with the announced preferences. These effects are stronger for discretionary investment changes. In the second part, the effect on governance of NBIM portfolio firms is analyzed. The problem is that NBIM may be correlated with the error term. As a solution NBIM is instrumented by NBIM in 2011. It is found that there is a 5 % overall improvement in overall governance. Most of this effect comes from firms that change their corporate governance.

In the second part, the discussant Oğuzhan Karakaş gives a short summary of the paper. The comments of the discussant first relate this paper to his research and to associated relevant literature. The discussant's research already found that "Active Ownership" is effective in improving the firm performance and governance. Hence the main findings of this paper are consistent with "Active Ownership". Another paper from the discussant finds that firms are subject to "Coordinated Engagements", and hence some of the effects that this paper finds may be not solely attributable to NBIM, but to collaborative investor efforts. A relevant paper documents that (i) NBIM opposes management more often than BlackRock does; (ii) NBIM is more active on Environmental and Social issues than Governance ones; and (iii) Delegated philanthropy is stronger than universal ownership in addressing negative externalities via institutional investor's engagement. Another related paper addresses the dual of the question in this paper: what are the changes in firms excluded by NBIM (as opposed to firms included by NBIM, as in this paper) and finds a negative return impact on the exclusion announcement. In the next step, the discussant provides comments on the analysis. First, the biggest reaction in the results seems to be over 2011-12, though the announcement of the Note was on November 2012: could firms respond such effectively to the Note in a month? Furthermore, in 2011 there is an unusually high number of discretionary exits: are these exclusions driving the results and could some of the firm's investors have anticipated the Note in 2011? The second comment on analysis relates to EIKON index scores: detailed discussion/ analysis of the EIKON scores would be helpful. Could other indices be exploited (environmental, social, governance)? The third comment on analysis was about the more detailed analyses of the NBIM investment strategy: the benchmark index is set by the Ministry of Finance on the basis of indices from FTSE Group and Bloomberg Barclays Indices, though the paper only refers to FTSE Group. Furthermore, the equity allocation in the strategic benchmark index has been changing over time, which could have an impact on the empirical results provided. Finally, the discussant provides suggestions/questions: Which components (out of 34) of governance score improve after NBIM involvement? How did the value, performance, risk and ownership of NBIM firms change after announcements? Are some analyses (inadvertently) forward-looking? Proxy voting agencies may also serve a similar function by setting/announcing certain ESG standards and voting accordingly.