# The Systemic Governance Influence of Expectation Documents: Evidence from a Universal Owner

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# Instutional Investors & corporate governance

- Institutional investors have multiple governance mechanisms to exert influence on their portfolio firms:
  - Negotiate with boards
  - Request board representation
  - Voting
  - Shareholder proposals
  - Launch proxy fights
  - …

- We analyze a new growing low-cost activism tool that aims to influence the entire portfolio of an investor: **expectation documents**

# Expectation Documents

- **Documents in which investors publish their expectations (preferences) on a particular topic, so firms in their portfolio address them**
- Topics: climate change, CSR, corporate governance…

- Special features:
  - New growing activism tool
  - Cost-effective
  - Influence the whole portfolio of an investor
  - Investors publicly commit and this may increase the impact on firms

# Expectation Documents

Which investors have used them?

- BlackRock, Norwegian SWF (NBIM), Vanguard, Japan's Government Pension Investment Fund, platforms such as the Climate Action 100+, PRI…

- Primarily, universal investors (large global investors that have a substantial share of all listed firms in their portfolio) that have limitations for active monitoring

# Expectation Documents

## Why universal investors?

- Investors can diffuse their preferences to the entire market (cost-effective)
    - Creates potential for systemic change
    - Can coordinate firms into a new equilibrium

- But, investing in a broad set of firms
    - May diminish influence as threat of exit is less likely
    - Reduces incentives for stewardship

Expectation documents are becoming a common tool to deal with this trade-off

- Interactions between expectation documents and active ownership characteristics
    - Complements: can exit and stewardship, reinforces expectation documents
    - Substitutes: Do expectation documents reach where other tools don't?

# Our research:

Use an unexpected change in the governance preferences of Norwegian Bank Investment Management's (NBIM) to see its impact on firm's governance.

- November 2012: NBIM releases an expectation document with emphasis on effective corporate governance.
  - Board accountability and composition
  - Equal shareholder voting

- **Research questions:**
  - Did firms react to the change in preferences?
  - Did NBIM really target its investment to its newly stated specific preferences?

# Main Findings

- Firms reacted by targeting the new governance preferences of NBIM
  - NBIM's influence:
    - grows with its share of firm ownership
    - uniform across the share of the firm in NBIM's portfolio
  - Heterogeneous effects informative about the complementarity of expectation documents with exit and stewardship

- NBIM's investment strategy aligns with the announced preferences. After the announcement:
  - entrants have better inherent governance
  - exits have worse inherent governance
  - portfolio returns: NBIM willing to trade-off returns vs. governance

# Contact

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