Fighting back

An interview with Eric Knight, CEO & CIO of Knight Vinke Asset Management.

Arguably Europe's best-known activist investor, Knight Vinke has seen its assets under management more than halve from around $2 billion to $800 million in the past two years. Despite that pressure, it is still influential, and is hoping to capitalize on rising demand for activism with a new, more liquid fund.

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Recently ensconced in smart offices in Mayfair's Hanover Square, Eric Knight and his team are buzzing from the announcement that Darty—a French electronics retailer the activist has owned a stake in for more than five years—is in takeover talks with Groupe Fnac for an all-share deal worth roughly 101 pence.

Back in 2010, Knight Vinke urged Darty's management to sell, but faced resistance and watched in disappointment as the company's arm of English stores, known as Comet, collapsed into insolvency and was sold without its pension liabilities. Knight subsequently joined the board in 2013, helping to pilot shares back up to 132 pence before resigning his seat. Unlike many other shareholders, the activist missed the opportunity to head for the exit, hanging-on while the stock swung back into the low 70's.

The fund will likely break-even after a bumpy ride, and Knight accepts there were missed opportunities along the way. "If there's one thing I regret it's that I didn't follow my own instinct, which would have been to push much harder at the beginning," he says.

The experience has also taught Knight to return to his preferred universe of targets—complicated large-cap companies with an array of seemingly competing stakeholders. Here, he suggests, information overload often obscures the true picture of a company.

The fund's philosophy is a challenge to two prevailing but contrary readings of financial markets—that they are efficient, and accurately price stocks based on their fundamental value; and that investors owning less than 1% of companies with large government holdings or influential stakeholders cannot possibly set the direction of travel.

"I say to my analysts all the time, our job is not to take something complicated and make it even more complicated," Knight says, presaging a short lecture on how even directors fail to understand even their own companies. "We try to simplify it, and it's by simplifying it to its very essence, that you can have the greatest sway with stakeholders."

Electrabel

Simplification takes a lot of hard work, and some Knight Vinke campaigns have involved thousands of man-hours and $2-3 million spent on research. In one famous example, Knight Vinke held an event for all of Belgium's mayors to discuss their shared stake in a joint venture in the country's main nuclear energy supplier, Electrabel, subsequently acquired by parent company Suez for $14 billion.

"I told them how much of a windfall they were going to get," Knight says. "There was an asset, which they owned 20% of, that was on the balance sheet for $2 billion. The idea was that they could build a lot of schools." Perhaps even more miraculous was the media interest. "We had a national debate at prime time in Belgium on the structure of the energy market there," Knight exclaims.

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Now, Knight Vinke has the opportunity to get a bit more creative. In June, it announced plans to launch a new fund aimed at private investors, with daily liquidity. Three months later, and the Knight Vinke Global Value Fund is being marketed with management fees graded from 1-2%, depending on invested capital. Knight is targeting $300 million in the near-term, and is applying for a UCITS license, which allows the fund to be marketed throughout Europe.

The shift is in part due to friction between Knight Vinke and its institutional clients. The firm bought out US pension fund CalPERS' stake, which provided its seed capital, in 2013—the tenth anniversary of their relationship. Earlier this year, the Texas Teachers' Retirement System terminated its management agreement with the fund.

For his part, Knight felt constrained managing large pots of institutional money—clients kept sweeping-out cash after each campaign, and were reluctant to let Knight Vinke go short, having invested in the fund as a long-only proposition. Returns, more volatile since the financial crisis, averaged 7.8% after fees at the end of September. The new fund will have no performance fees, according to a term sheet seen by Activism Monthly Premium.

Nervous about the state of the markets, Knight has only put one investment into the new fund, but will add others (probably up to six) as they become more attractive. "We see significant opportunities for value creation in European banking and energy," he says. Food, chemicals and luxury goods companies are all on Knight Vinke's radar too, but much will depend on how the remainder of 2015 plays out in the markets.

The activist even has a new campaign to get revved-up over, although Knight is reluctant to disclose details. Among the many thick folders of research on Knight Vinke's shelves, built up over 12 years of research, a new chapter is waiting to be opened.

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"I told them how much of a windfall they were going to get," Knight exclaims. "There was an asset, of which they owned approximately 50%, which was on the balance sheet for €2 billion but had a value which we estimated at over €18 billion." The Belgian stake was subsequently bought out by the company's owner, France's Suez, delivering a major windfall. Knight savors the intellectual victory almost as much as the financial one. "We had a national debate at prime time in Belgium on the structure of the energy market there." ■

UBS

"This is the annual report of UBS," Knight says, waving the tome. "This year it's 1,150 pages of very dense, complicated ink. How can you as a board member hope to know what's going on there? And of course you've got a quarterly report, which came out two weeks later, which is this thick [around 400 pages]. And of course you need to have read the one on Credit Suisse and JP Morgan and Deutsche Bank and HSBC to see how it compares."

The European model of universal banking has been justified by the promise of synergies that are rarely made explicit, Knight argues. Recently, however, regulators have been applying pressure on global banks to ring-fence different businesses, so that UBS's new structure actually mirrors the split between private and investment banking that Knight Vinke has been calling for, albeit under the umbrella of a single parent company—tectonic plates moving apart, Knight says. That means greater transparency, and a chance to apply yet more pressure, he adds. "We're into our third year and we're finally getting the data we need to calculate what these subsidies actually are."