



## United Airlines: A Case in Shareholder Activism

*It appears that United Airlines (NYSE: UAL) can't catch a break when it comes to stabilizing its top leadership. What seemed to be a fresh start following the return of CEO Oscar Muñoz after undergoing a heart transplant, abruptly shifted to an activist shareholder dispute.*



On March 14, 2016, Oscar Muñoz returned to his job as Chief Executive Officer of United Airlines following a heart transplant. At the same time, activist investors, Altimeter Capital Management (Altimeter) and PAR Investment Partnership LP (PAR), who jointly own approximately 7.1% of the company, upped their activist campaign to influence board decisions, citing their desire to see changes in board composition, shareholder value enhancement and corporate strategy. Now, Muñoz faces a bitter shareholder activism dispute along with a host of pre-existing operational and performance issues at United.

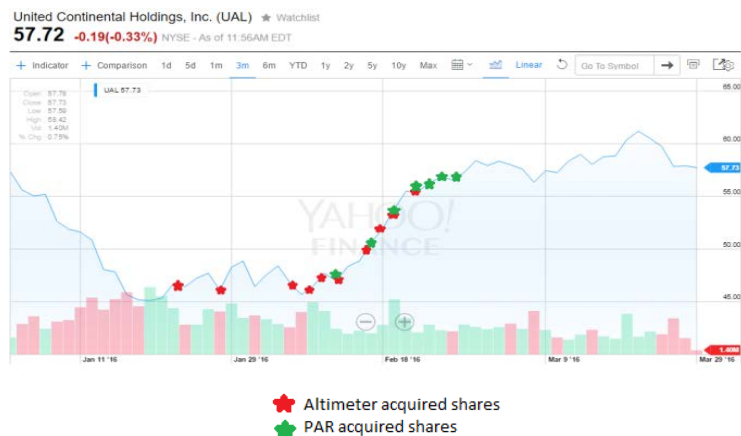
The problem began in August 2015 when concerns about succession planning and insufficient disclosure by the board escalated after former and well-liked CFO, John Rainey, left United to join PayPal. This unpopular news was followed by the resignation of CEO, Jeff Smisek, amid a rising scandal related to the airline's dealings with the Port Authority of New York and New Jersey in September. The company acted quickly, replacing Smisek with Oscar Muñoz, formerly President and Chief Operating Officer of CSX Corporation, a premier freight transportation company.

The new President and Chief Executive Officer, Mr. Muñoz faced a long list of challenges, including: low punctuality indicators, widespread technology glitches as well as poor customer service. All of the above added to the situation brought on by Altimeter and PAR, two hedge funds with no prior record of shareholder activism. To further complicate matter. In October 2015, Mr. Muñoz suffered a heart attack and this past January, he underwent heart transplant surgery, leaving the company leaderless during a very crucial phase.

### Who are Altimeter and PAR?

Altimeter, founded in 2008 and headed by Brad Gerstner, describes itself as a global investment firm managing both public and private funds focused on the airline, travel, technology, internet, software and consumer sectors.

Currently, Altimeter has a 3.1% stake in United and has been an investor for over six years.





PAR Capital Management, led by Founder and CEO Paul Reeder, manages a private investment partnership. The firm was founded in 1990 and it first acquired United shares in November 2015. In January 2016, when the stock reached a 12M share price low, PAR upped its total stake in the company to 2.4%.

Currently, the funds claim to have a combined 7.1% of the company's outstanding common stock; representing just over US\$1.5 billion. This figure surpasses the Vanguard Group's 7% stake.<sup>1</sup>

**What do they want?**

On March 8, 2016, Altimeter and PAR filed a 13-D with the SEC, which included a letter addressed to United's Board of Directors. In the filing, the activist shareholders cited their desire to "revitalize an underperforming board" and included 6 nominations for the company's Board of Directors, which would be led by Gordon Bethune, former CEO of Continental Airlines. The nominees included former board members of iconic travel industry companies, such as Orbitz Worldwide, Homeaway and Continental Airlines, who would be able to "bring meaningful experience, objective insight and powerful change to United".

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

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**SCHEDULE 13D**  
Under the Securities Exchange Act of 1934  
(Amendment No. 2)\*

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**United Continental Holdings, Inc.**  
(Name of Issuer)

Common Stock, \$0.01 par value  
(Title of Class of Securities)

910047109  
(CUSIP Number)

PAR Capital Management, Inc.  
Attn: Steven M. Smith  
One International Place, Suite 2401  
Boston, MA 02110  
(617) 526-8990  
(Name, Address and Telephone Number of Person Authorized to Receive Notices and Communications)

March 8, 2016  
(Date of Event which Requires Filing of this Statement)

In essence, Altimeter and PAR Capital seek to overhaul United's Board. Their main concerns, as cited in the letter, are:

1. United has a **Clear Record of Sustained and Substantial Underperformance**
2. United has an **Underqualified, Ineffective, and Entrenched Board**
3. United **Urgently Needs a Course Correction**



<sup>1</sup> According to Thomson Reuters data.

An activist investor is an individual or group that purchases large numbers of a public company's shares and/or tries to obtain seats on the company's board with the goal of effecting a major change in the company. ---  
*Investopedia*

Activist investing has become a common and acceptable means of expressing shareholder views and concerns. Investors have not only become more sophisticated, but access to information is now much easier than before.

As a result, activist campaigns are becoming more commonplace and the number of target companies continues to grow globally. Institutional investors, company executives and boards are learning how to work together for the long term benefit of the company. As such, it is not fair to perceive activist investors as the “bad guys” and the company’s management as the “good guys”; rather, it is important for companies and their boards to adapt to the changing environment and be prepared for the new dynamic.



Public company executives and board directors have recognized the importance of taking a more proactive approach and adopting a range of structural changes within the company. For this, i-advize strongly recommends that its clients cultivate an **activist prevention strategy**. The company must be prepared to address investor concerns and articulate a plan for righting corporate situations *prior to the rise of an activist situation*. Here are the most common measures i-advize suggests to **preventing shareholder activism**:

1 – **Identify vulnerabilities at the company** and seek to remedy them with the support of the Board of Directors. Typical vulnerabilities that leave a company open for activism activity include but are not limited to:

- ✓ Poor market/financial performance among peers
- ✓ Suboptimal capital structure
- ✓ Corporate governance – issues of succession and management changes can leave the company vulnerable
- ✓ Cash resources with no clear strategy of how they will be utilized
- ✓ Sudden decline in share price
- ✓ Perception of lack of transparency
- ✓ Slowing innovation or launch of new products/services

2 – **Maintain strong employee relations** – In the case of United, the union representing United’s 12,000 pilots and flight attendants threw their support behind the airline against the activist shareholders. The pilots cited that the “...*coup attempt, being done for their own benefit, and without publicly stating their intentions for the future of the airline, unnecessarily distracts all employees from our commitment to improve customer service and grow United Airlines.*”



However, not all companies are this lucky, unless they have invested in strengthening long-term employee relationships.

Activists seek weak areas within a company to demonstrate the need for their proposed changes. Activists may perceive that employees are unmotivated to strive or unwilling to provide good customer service as a result of their discontent with management, and use this argument as reason for the company's underperformance.

Furthermore, it is important to note that personnel are also stakeholders in the company that could jointly own large chunks of stock resulting from Employee Profit Sharing programs. Their vote is important when it comes to making approving proposals at shareholder meetings. To maximize this, management can include employees in its strategy and use their support to make decisions that are for the long term good of the company and its employees.

Strong bonds between management and employees contribute to reaching strategic goals and achieving a good operational performance. Positive operational results support management when demonstrating to shareholders that the current strategic vision and leadership are, in fact, contributing to the company's growth.

3 – **Continuously monitor shareholder base** – look out for investors who have a history of activist activity<sup>2</sup>. While this was not necessarily the case in the United situation, (it was the first time that these hedge funds had come out as activists), most activist shareholders *do* have a track record of being more vocal in the stocks that they own. Periodically monitor institutions that acquire shares in your company and contact top shareholders regularly to understand their issues and address their concerns. You may need to engage a stock surveillance firm annually in order to obtain an accurate updated shareholder list to work with.

When holding discussions with shareholders, be sure to articulate the benefits of the company's current strategy and ensure that they understand and are on board with your thinking. Such an effort can minimize the company's odds of becoming a target.

4 – **Remain Competitive** – Activists continuously target companies that they believe are not living up to their full growth potential. This includes a low relative stock price versus peers, stunted growth, declining market share, etc. Activists like to "invest" in companies that are priced low but that have the ability to turn around and increase in value. In some cases, the activist may even seek to have the company sold to or merged with a larger company. The M&A transaction can be extremely lucrative from a shareholder's point of view.

5 – **Keep the Board informed** – Also ensure that the board obtains relevant and concise company information, particularly with regards to information related to growth potential, product/business lines, market share, competition, and areas of weakness and improvement. The board's ability to assess the company's main weaknesses and investor concerns can help them understand the weak points and support management's actions and goals. The primary function of the board of directors is to oversee management for the good of the company. Oftentimes, this mission is forgotten and the board reviews information without really questioning management decisions or strategy. Review your board composition often and make changes when necessary to keep the team fresh and motivated. An excellent tool to accomplish this is the *Annual Market Perception Study*.

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<sup>2</sup> For a list of activist funds in the U.S. please contact your account representative at i-advize Corporate Communications, Inc.



6 – **Maintain transparency** – A major part of the investor relations and corporate communications function is management’s ability to be forthcoming with regards to its corporate strategy. As such, transparency means the ability of management to address market concerns with a clear strategic plan and objectives aimed at overcoming challenges. The plan should clearly delineate the company’s strategic vision, its growth plans, R&D goals, as well as corporate governance objectives.

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**A Blueprint for Responding to Activism**

With the popularity of shareholder activism on the rise, it is important to mention that no company is exempt. Even those who engage in all of the preventative measures can find themselves in an activist predicament one day. In the event that this happens, following are some tips from the pros:

- a. **Seek legal advice:** Legal experts can foresee certain consequences (including those in the strategic activist handbook) and can help the company avoid saying or doing something that can aggravate the situation with an activist.

When seeking legal counsel, examine their background – who will be working on your case? Have they been involved in other activist campaigns? What were the results and how long did the process take?

No two activist situations are the same. Some can be resolved with a simple intermediation, while others can drag on for months and years. Having top legal support can make the process less painful and hopefully, shorter.

- b. **Don’t dismiss activist ideas:** Although an activist attack can be described as a “battle”, it is important to take into consideration the activist’s proposals - after all, their intention is generally to increase the value of the company for the benefit of shareholders. While activists can be disruptive, they can also be intelligent and motivated investors with a clear ability to identify weaknesses overlooked or not addressed by boards or management. Therefore, it is important to be open minded and objectively evaluate their ideas.



When it comes to analyzing activist proposals, management should involve the activist as well as other relevant areas of the company. The discussion does not need to have a “right” or “wrong” answer but should be a discussion of how it could affect other areas of the company. Entertain opinions and discuss. Thoroughly analyzing each proposal and implementing those ideas that make sense will help you come up with a proposal that keeps all parties satisfied.

- c. **Prevent a proxy battle:** A proxy battle is an unfriendly contest for the control over an organization. The event usually occurs when corporation’s stockholders develop opposition to some aspect of the corporate governance, often focusing on directorial and management positions. By removing existing board or management members, the





activist launching the proxy fight can establish a new team that is more aligned with their objectives.

A proxy battle is seldom beneficial for the company as it can significantly impact finances by raising legal expenses. Most importantly, it can be a drain on the company's time and efforts and can be a distraction to management, which can result in losing sight of the company's strategy and direction. Note that activists tend to cash out their holdings shortly after their demands are accepted or rejected, so their true commitment



to the company's future success is in question. Companies that easily allow activists to win over the board risk losing the commitment and engagement of their employees and customers, jeopardizing the company's competitive position.

Therefore, it is important that companies continue to be open to negotiations in order to prevent a proxy fight. If activists knock your door, hear them out. Closing doors will only provoke them to immediately initiate a proxy battle.

**d. Communicate:** By telling a clear story and openly communicating with investors, companies can ensure that their strategic agenda remains front and

center. The IRO role becomes essential in addressing shareholder concerns directly and in a timely manner. For this, take advantage of the communication tools that are readily available:

- **Press Releases** - Address any activist proposal that has been made public; clearly state the activist position and the company's position and reasoning. Publicly acknowledge that activist suggestions are being analyzed and that the company is willing to be open and collaborative with all shareholders. Ensure shareholders that the company is handling the situation and that this won't disrupt operations. Lastly, keep the investors informed on updates regarding this impasse.
- **Conferences and investor days** - Use group events as an opportunity to highlight the company's strategy and leadership. Keep the market abreast on internal initiatives as well as competitive strengths that make the stock a worthwhile investment. What made them an investor in the past is in the past now, group meetings are an opportunity to make investors fall in love with the company all over again.
- **Media**- Use mass communications as a way to reach the general market, particularly if you have an important retail investor base. Speaking with television outlets, print and internet media gives the company an invaluable opportunity to sell itself and its leadership with the mass market with a relatively low time investment.
- **Social Media and Corporate Web Site** - The same as with regular news media, social media allows the company to reach a more varied audience than regular group meetings. Use social media to inform



customers as well as investors regarding initiatives at the company. For instance, create a Twitter account to broadcast your news releases and quarterly conference calls. Finally, make sure all communications addressing the activist campaign are available on your IR website. Materials include presentations used on conferences, investor days, roadshows and all press releases used to update the market.

### Ongoing self-assessment

Even after the activist campaign is over, it doesn't mean that another possible claim is not around the corner. Remember, as management, it is your duty to shareholders to ensure the long-term viability of the company's mission and strategy. Going forward, implement internal reviews and assessments to guarantee that the business is no longer vulnerable to activist acts. Hold regular meetings with board members and management to thoroughly discuss market concerns, and come up with a strategic plan to address them.

### A final note on United

Clearly, the unfortunate circumstances surrounding the former and current CEO's scandals and health problems contributed to enabling shareholder activism to take root. As of today, however, it seems as though United is on the right track to handling the situation fairly well. For one, the demands from the investors seem manageable and the company's employees --- and even some members of the media --- have sided with the company. To United's credit, it has seemingly taken *all* the proposals seriously and has even engaged in communications with its activist shareholders on a number of occasions. Specific proposals made by PAR and Altimeter, such as certain board appointments for example, have been partially implemented.

In terms of market communications, United has made efforts to update with regular press releases on the matter and statements made to the media. It has also attended industry conferences focusing its presentations on corporate strategy and vision. And while the pressure from shareholder activists is not likely to go away any time soon, at the time of this whitepaper, it has not prevented the company from conducting its business as usual. How it ends remains to be seen and we are left to wonder what United could have done to prevent this situation from even occurring in the first place.

***For more information on Investor Relations Activities, including shareholder activism preventative measures, contact us:***



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