Making sure your vote does not count: green activism and insincere proxy voting

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Motivation

- ESG activist investing
  - Proxy voting
  - May hurt firm profit and market value
  - Becoming popular in last decade
- Pivotal voters are universal owners
  - Large institutional investors
  - Holding both targeted firm and many other firms
  - BlackRock, State Street and Vanguard cast about 25% of votes

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- Strategic green proposal voting by universal owners
    - Some universal owners may have green preference
    - Voting decision has reputation consequence
- Timely topic, some counter intuitive results
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The Model in a Nutshell

- Static economy, three groups of agents:
  - Activist fund (initiates green proposal)
  - A mass of atomistic small shareholders
  - K universal owners
- All agents are risk-neutral, may or may not care about environment
- Timing:
  - Activist fund purchase shares to initiate green proposal
  - Green proposal, if pass, lower the firm profitability
  - Small shareholders set the price, based on the eq. chance of green proposal pass
  - K universal owners voting simultaneously, with private type
- Focus on scenarios:
  - Activist fund always proposes
  - Universal owners are decisive

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- Main friction: Reputation cost
  - Reputation cost only depends on your vote
  - Firm value depends on all votes
- Brown investor may want to vote yes to save reputation cost
- No collusion, no public information about type
  - Trade off chance of proposal pass and reputation cost
  - Multi equilibria arise
  - Focus on pure strategy potential maximizing: all universal voters can do better if they change strategies together
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Interesting Results

- More concentrated reputation costs increases pass chance
  - High reputation costs almost sure vote yes
  - Very hard for other brown investors to win
  - If some voters choose the opposite, other voters are discouraged
- Pass chance is not monotonic in γ
  - Given the number of "no" voters, pass chance increasing in γ
  - Higher γ may introduce more "no" voters
  - When voters are confident, they don't vote
- More universal owners
  - Pass chance increases if $\gamma > \frac{1}{2}$
  - More difficult to coordinate
  - Pass chance decreases if $\gamma < \frac{1}{2}$
  - More "no" draws

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- Activist fund: to initiate the proposal
- Small investors: to determine the price
  - No discussion about proposal initiation choice
  - The exact change of price (p_0) is irrelevant for the voting discussion
  - All you need is a proposal that may hurt firm financially
- Both are mechanic in the model
- Drop those two!
- Clean and focused model setup
- Avoid strong assumptions on activist funds and small investors voting

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- In model, universal owners are decisive and the major uncertainty is their type
- Decisive: make sense given how large they are
- Private type and reputation cost
  - They invest in many firms
  - They vote many times per year
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January 25, 2022

Click for PDF

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These pronouncements from the "Big Three" asset managers reflect a number of common themes, including an emphasis on climate and the transition to a Net Zero economy, diversity at the board level and throughout the workforce, and effective human capital management. Links to the BlackRock and Vanguard voting policies for 2022 are below. State Street's voting policy updates span several documents that provide guidance on areas that State Street views as focal points for the coming year. Links to these documents are also below.

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- Reputation, essentially, is a belief updating
- In model, universal owners have same γ, but different reputation cost
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    - High γ, high reputation cost
    - It may simplify the analysis because reputation cost is endogenous
    - Some result may change: concentrated reputation cost

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Comments IV: Voting Mechanism

- Simultaneous voting with private type fits individual voting
    - Hard to communicate in a large group
    - Hard to have real-time update on voting progress
- However, there are many other voting frameworks may fit better for the universal owners
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- Recent trend on institutional Pass-Through voting


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Conclusion

1. Important topic, policy relevant!
2. Simplify the model setup
3. Blockholders v.s. Universal Owners
4. More discussions on voting mechanism choice
5. Good luck!