Does Coordinated Institutional Activism Work?
An Analysis of the Activities of the Council of Institutional Investors

by

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Executive Summary

The Council of Institutional Investors is a group of public and private pension funds which collectively own over $800 billion in financial assets within the United States. The Council has provided a forum for these funds to coordinate and communicate with each other on a variety of matters including activism programs aimed at facilitating solution of problems in underperforming portfolio firms. The Council has issued a focus list of poorly performing firms for each of the last five years to its members who have the discretion to pursue activism programs. These lists have included well-publicized underperformers such as IBM, Kodak and Sears along with a variety of less known cases. This study documents the performance of 96 firms which appeared on the Council's focus lists in 1991, 1992 and 1993 relative to several control groups. Firms on Council focus lists experience poor share price performance in the year before before being included on a focus list. In the year after being listed, these firms experienced an average share price increase of 11.6% above the S&P 500. Given that the mean equity market value of Council listed firms was $3.42 billion we estimate a total abnormal dollar gain of these firms of $39.7 billion. This increase is broadly consistent with the view that coordinated institutional activism creates shareholder wealth.

1. Introduction

Perhaps the most important development in the market for corporate control in the 1990s has been the emergence of increased activism by large institutional shareholders such as the California Public Employees Retirement System (CALPERS), the Florida State Board of Administration, TIAA-CREF and the Wisconsin State Investment Board. These institutions have attempted to pressure board members of many leading corporations to improve performance and/or remove anti-takeover obstacles.[1] This pressure has taken place through public and private channels: Publicly, institutional investors have joined dissident shareholders in voting against management on proxy proposals, while privately, they have engaged management in discussions about ways to improve performance.[2]

Recently, several studies have found that this type of public monitoring has little effect of shareholder value (e.g. Gillan and Starks (1995) and Karpoff, Malatesta and Walkling (1995)). There is even less evidence of the efficacy of 'quiet' pressure. Given that the current era of corporate governance activism is characterized by relationship building rather than tender offers, by board pressure rather than by financial pressure and by quiet diplomacy rather than highly publicized takeovers (Pound (1992)), this type of monitoring may, in fact, be more valuable.

This study investigates whether coordinated and primarily 'quiet' governance activism generates value. We are motivated by oft-voiced concerns that institutional activism is misguided and unlikely to be effective. For example, business leaders have argued that large pension funds lack the expertise and ability to serve as effective

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[1] For example, CalPERS and the Pennsylvania State Employees Retirement System (PSERS) worked together with other funds to pressure the board of Eastman Kodak to increase shareholder value in 1993. Kodak committed to sell off Eastman Chcmical and the Board eventually replaced CEO Kay Whitmore with George Fisher.

[2] The *Wall Street Journal* reported that Robert Monks launched his attempt to gain a seat on the Board of Directors of Sears at a meeting of the Council of Institutional Shareholders (4/5/91) and later the CII supported Monks in a campaign to voice displeasure with Sears management by abstaining from a vote for unopposed seats on the Board of Directors (5/13/92).

monitors in the market for corporate control. Furthermore, state pension funds are subject to political pressures to back off of activism and aid the political objectives of local politicians (e.g. Business Week (1991)). Roberta Romano (1993) argues that it is very costly for managers of public pension funds to navigate around the "shoals of considerable political pressure to temper investment policies with local considerations, such as fostering in-state employment, which are not aimed at maximizing the value of their portfolio's assets.” In a study of state pension boards from 1987 to 1989, she found that activist state pension boards earned returns no greater than those of other funds. Efforts at institutional shareholder activism may also be hindered by a lack of accountability, absence of appropriate incentives and free-rider problems due to the fact that any one institutional shareholder typically holds a percent or two (at best) of the shares of a large corporation (Admati, Pfleiderer and Zechner (1994); Monks (1995) and Murphy and Van Nuys (1994)). To date, the great majority of large institutional investors in the United States have maintained a passive stance on corporate governance issues (Wahal (1995, p. 9)).

One possible way for institutions to reduce free-rider problems among themselves and to side-step political pressure is to create an organized third party monitoring organization. Such an organization can serve as a focal point for diffuse investors and, perhaps, give investors more credibility in challenging management than they could have separately. In principle, organized institutional shareholders can exercise significant clout at a fairly low cost because there are economies of scale in activism (Black (1990)). A variety of institutional investor organizations exist including the Council of Institutional Investors and the Committee on Investment of Employee Benefits Assets of the Financial Executives Institute.

This study focuses on the efforts of the Council of Institutional Investors (CII). The CII is composed of public and private pension funds which collectively own over $800 billion in financial assets. The Council provides a forum for funds to share information and to jointly monitor corporate performance, executive pay and governance related issues. We focus on the activities of the Council because of its high profile as a corporate monitor during the early 1990's. For each of the past five years, the CII has circulated a list of firms that are identified as performing poorly on one or more of the three dimensions mentioned previously. While the CII staff is responsible for compiling and distributing the list, the organization itself does not engage the management of these firms to change policy.[3] This list may affect the firm's involved by helping Council members to coordinate their activities.[4] In addition, negative publicity associated with publication of the list may add urgency to internal efforts to achieve a turnaround and legitimize efforts of independent directors to push for change.

We investigate whether firms which have appeared on focus lists of the Council of Institutional Investors experience improvements in performance. In the process we also examine performance of these firms prior to appearance on focus lists and operational changes which take place before and after listing on a Council focus list. Evidence that firms experience improvements in operating and stock market performance subsequent to inclusion on the CII focus list would be consistent with the view that coordinated monitoring and 'quiet' governance activism by institutional investors is effective.

Our main results show that firms placed on Council focus lists in 1991, 1992 and 1993 were historically strong performers which experienced earnings declines in the four years before being listed. Subsequent to being listed, we find that these firms experience substantial recoveries in both profitability and share price. While consistent with the view that activism undertaken by members of the Council of Institutional

[3] The Council has never removed a firm from the list because of lobbying and counterarguments. However, starting in 1994, the Council has allowed listed firms to respond with a letter that is distributed to all members.
[4] An in-house survey found that many Council members contacted management of firms they invest in that appeared on focus lists.

Investors is effective, it is also possible that these firms were undervalued or in a risk class likely to receive particularly high returns as a risk premium. To address this possibility, we compare the performance of focus list firms to portfolios matched on the basis of previous performance, size, book-to-market ratio, and industry. We find that focus list firms experienced better market and operating performance in the year subsequent to inclusion on the CII focus list than these comparison firms. This pattern is consistent with the view that institutional pressure accompanying appearance on a focus list generates real operational results in the corporate community.

Our results differ from those in several recent studies which find little effect of institutional activism carried out through shareholder proposals. (See Gillan and Starks (1995), John and Klein (1994) and Karpoff, Malatesta and Walkling (1995)). A related paper by Wahal (1995) finds no evidence of improvements in share price performance or profitability following targeting of 87 firms by nine leading pension funds (he follows firms which were targeted in consecutive years from the first year targeted forward only). In fact, he finds that targeted firms experienced statistically significant continued *declines* in long-term share price performance after targeting. The difference in findings between Wahal's study and ours may be partly attributable to the fact that his paper contains a relatively small group of firms that were targeted for performance-related reasons and a large group of firms that were targeted through shareholder proposals.[5] We also focus on a more recent time period than the four above-mentioned studies. Strickland, Wiles and Zenner (1995) find a small positive abnormal return (0.93% or $50 million per firm) around the agreement date for resolutions sponsored by the United Shareholders Association (USA), a group of small investors, that targeted numerous firms up through 1993.[6] Two studies of CALPERS activism by

[5]Wahal finds that firms which were targeted for performance reasons experienced positive share price reactions in a seven day period around proxy mailing and/or release of a target list.
[6] The USA last operated in 1993. Even though the gain per firm was not large, the total contribution of efforts of the USA are significant. Strickland, Zenner and Wiles estimate that the value contributed by

Nesbitt (1994) and Smith (1995) find a small but statistically significant long-term share price improvements afterwards.

This study differs in several key regards from previous work. First, we examine *coordinated* shareholder activism efforts rather than efforts of a *single* pension fund. Second, we only look at firms relative to when they appeared on a Council of Institutional Investors focus list. This is important because a potential problem with studies that focus primarily on public governance events (e.g. proxy proposals) is that the most recalcitrant (and least likely to improve) firms are the most likely to be targeted in a public forum. It might very well be that management teams are most responsive to activism efforts which are private and carried out in the context of a long-term relationship. Because firms are not consulted before they are selected to be included on Council focus lists, our sample includes firms which may be responsive to quiet diplomacy that many not have been examined in other studies.

2. The Sample

2.1 Sample Selection

We examine all firms which appeared on focus lists issued by the Council of Institutional Investors in 1991, 1992 and 1993. These lists are made public at the Fall meeting in early October. While the firms on these focus lists are usually mentioned in the media, we have found that past news coverage of the focus lists has been slim. We date release of these lists on the first day of October. In 1993, the Council placed several firms on its focus list at other times. We date the listings of these firms from first mention in the media (based on a search of all periodicals in *Nexis*). In total, we have 99 separate listings in the 1991-93 period (performance data are missing on CRSP and COMPUSTAT for two of these firms). There are fewer firms than listings

USA efforts and propositions totalled more than $1.3 billion (compared to a cost of less than $25 million of running the USA).

because some firms were listed in consecutive periods. The appendix to this paper lists all firms which were placed on focus lists in the 1991-93 period with listing dates and subsequent one year raw total shareholder returns.

2.2. Data

Information on firm's performance was obtained from the Standard and Poors COMPUSTAT II PST tapes. Data on firm stock price performance were obtained from the CRSP tapes issued by the University of Chicago.[7] Returns are compounded daily and adjusted for splits. Dividends are assumed to be reinvested in the stocks under consideration.

2.3 Comparison Group Portfolios

A major goal of this study is to document the stock market performance of firms included in the Council of Institutional Investors' annual focus list. It is critical that any measure of performance be benchmarked appropriately to ensure that our results do not mirror a risk factor or other known anomaly. We create benchmark portfolios on the following dimensions: size, market risk, short-run past performance, long-run past performance, the book-to-market ratio, and industry performance. In all cases, a selection criterion was that the matched firm had to trade for a full year after selection.

The first logical comparison group is the market as a whole. We report stock market performance for the portfolio of firms in the Standard and Poors 500. The S&P 500 portfolio also acts as a control for both market capitalization and market risk. Table 1 describes the CII focus list sample with respect to market capitalization and

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[7] CRSP data are issued with a lag which means that we have not been able to include firms on the 1994 focus list in this study. We have examined the share price performance of these firms using a Bloomberg terminal and S&P industry indices. The mean post-listing one year return for the 20 firms on the 1994 list was 35.1% versus 29.8% for the S&P 500 and 23.2% for the industries of listed firms.

age. The median market capitalization of firms in the sample is $3,421 million. These are primarily mature firms, with an average of 31 years on the CRSP tapes (out of a possible maximum of 68 years). Over 82% of the firms also appear in the S&P 500. The large size of sample firms also suggests that they exhibit risk characteristics similar to the market as a whole; in fact, the mean and median Beta estimates for our sample are 1.06 and 1.04 respectively.[8]

As a side note, we can infer from Table 1 that the 1993 sample is somewhat different from the prior two years; the average market size falls by half, the number of NASDAQ firms increases, and the percentage of firms included in the S&P 500 falls from the over 90% to just over 70%. The staff of the Council of Institutional Investors has indicated that the procedure for choosing focus list firms changed in this year (firms were selected from a larger universe by a company called Institutional Shareholder Services). By 1993, the strategy for inclusion weighted more heavily on market underperformance than in prior years. The dynamic nature of the firm selection process may make it more difficult to capture the relation between coordinated institutional activism and increased performance. It also provides us with a natural robustness check. Were our results to hold across time periods, it would it would be hard to argue that they could be attributed to a special risk characteristic identified by the screens.

We also employ a benchmark portfolio of firms which were matched to those in our sample by their return in the year before appearing on a Council list (SRM). This is the short-run match portfolio. This benchmark portfolio allows us to control for the possibility that firms on Council lists perform differently than the S&P 500 because a prior downturn in market value which is reversed or extended in the post-listing year. Zarowin (1991) finds a market anomaly where firms which underperform

[8] We estimate betas using the market model and five years of monthly return data. The mean (and median) Beta estimates for the three sample years are 1.25 (1.17), 0.99 (1.01), and 1.07 (1.01) respectively.

the market are likely to reverse themselves in the following year. Jegadeesh and Titman (1993), on the other hand, find the opposite. In particular, they found that firms which have done well in the immediate past continue to do so (consistent with momentum theories of market movements).

Another benchmark portfolio controls for past long-run movements (LRM) in the share price of firms on Council lists. We employ this benchmark to allow ourselves to check whether any abnormal performance of firms on Council lists reflects the long-run share price reversal effect noted by DeBondt and Thaler (1987). Each firm in our sample was matched with the NYSE firm which had the closest total market return to it over the preceding four years.

To control for a potential industry effect, we match each firm in our sample to all firms on the CRSP NYSE/AMEX tape with the same four-digit SIC code. In all cases, the industry-matched portfolio had a minimum of four firms for each company on the CII focus list.[9]

Finally, we employ a book to market ratio benchmark. Firms are matched with NYSE firms with the closest book to market ratio in the first accounting period ending before listing by the Council. Controlling for the book to market effect allows to remove any risk/anomalous behavior associated with distress as noted by Fama and French (1990).[10]

3.0 Operating Performance

[9] Kahle and Walkling (1995) find that CRSP SIC code classifications differ from those of Compustat 80% of the time at the 4-digit level. Concerned that our results using industry portfolios might not be robust, we also benchmarked against S&P industry portfolios (obtained from Bloomberg). Our qualitative results were the same using both approaches. Focus list firm net of industry performance was higher when we used the S&P industry portfolios.

[10] There is little persuasive evidence that the book to market effect found in the data behaves like a normal risk factor (see Lakonishok, Shleifer and Vishny (1994) and Daniel and Titman (1995)). It may very well be that governance activism plays a role in the book to market effect.

Table 3 describes the operating performance of firms on Council of Institutional Investors focus lists. For our purposes, we standardize operating cash flows (Sales - Cost of Goods Sold - Selling, General and Administrative Costs + Depreciation) by the book value of assets.[11] Because of data constraints, operating performance from year minus-3 to plus-1 is only available for the 1991 sample. We cannot calculate operating performance for year plus-1 and years zero to plus-1 for the 1992 and 1993 samples respectively.

Generally, we expect the CII sample to have low operating cash flows by the time these firms are included on the focus list (year 0). We have no clear hypothesis predicting operating performance in earlier years. This underperformance may be expected to be persistent in prior years to the extent that some of the firms are chronic poor performers and show up on the CII list in successive years. Conversely, a quick deterioration in operating profits may have been the event that precipitated this firm's inclusion on the Council's list. Although significant improvement in operating cash flows in year (+1) would lead to the conclusion that coordinated activism increases wealth, the literature suggests that market prices lead increases in operating performance by many years (see Easton, Harris and Ohlson (1992) and Ritter (1993)).

Table 3 reports operating cash flows as a percentage of assets at book of firms selected by the Council of Institutional investors in 1991, 1992 and 1993. The table also compares focus list firms' operating cash flows to firms in the short-run performance (SRM), long-run performance (LRM), and book-to-market (BTM) matched portfolios and the S&P 500.

Firms on the Council of Institutional investors lists generally exhibit depressed performance in the three years prior to inclusion on the focus list. The median operating cash flow for CII firms falls from approximately 20% to 15% of firm value

[11] Because the COMPUSTAT PST tapes do not adjust for fiscal year, we make the following adjustment; if the fiscal year ends in calculate operating performance for year 0 using year 0 data. Otherwise, operating performance for year 0 is calculated with COMPUSTAT data for year 1.

from year (-3) to year (0) for the 1991 and 1992 samples. This decrease is approximately 40% greater than for the SRM portfolio, 400% greater than the LRM portfolio, 20% greater than the BTM portfolio, and 46% greater than for the S&P 500 portfolio. Furthermore, most of the deterioration in cash flows occurs between years (-1) and (0). Operating cash flows fall 22% and 36% in this year for the 1991 and 1992 samples respectively. This confirms our expectation that firms selected by the Council of Institutional Investors experience a more rapid decline in operating performance than firms with similar risk characteristics just prior to inclusion on the focus list.

Cross-sectionally, there is little evidence that the operating performance of CII focus list firms is different than any of the benchmark portfolios. Any difference that may exist would be obscured by the low power of the test due to small sample size. Casual observation indicates that the median firm in the CII sample outperforms the median benchmark firm in the three years prior to listing, but exhibits a sharper decline in operating cash flows in year (0).

4.0 Share Price Performance

4.1 Pre-Listing Performance

We report the stock performance of the CII and benchmark samples prior to the year of listing for two reasons: first, we want to describe the economic condition of focus list firms before selection relative to risk-based benchmarks. Second, comparing short and long run performance of the CII sample allows us to document whether how well the SRM and LRM portfolios match the prior performance of the CII sample.

Table IV reports the share price performance of firms before being listed by the Council of Institutional Investors for the four year period preceding listing. Firms are also compared to the short-run prior performance (SRM), long-run prior performance (LRM), book to market (BTM), industry matched (IND) and S&P 500 benchmarks. Holding period returns are calculated using daily returns, assuming the reinvestment of dividends.

We know stock price performance is a key attribute considered by the Council of Institutional Investors when selecting firms for its focus list. Not surprisingly, listed firms exhibit mean (and median) share price performance which is substantially below that of the S&P 500 firms (10.3% versus 58.6%). Mean holding period returns are also significantly below those earned by other firms in the same industries (38.7%) and a set of firms matched on book to market ratios (47.7%). The portfolio based on matching long run performance reports holding returns of the same magnitude as the CII sample.

To check the quality of our short-run match we compare the one year prior performance of listed firms to other benchmarks in Table V. Council-listed firms had mean one year pre-listing holding returns (4.9%) which was very similar to the mean performance of firms in our one year performance benchmark (5.0%) but far below that of firms in the long-run performance (22.8%), book to market (21.5%) and S&P 500 (17.3%) benchmarks. The evidence presented does not indicate whether the

Council puts more weight on long-run or short-term performance measures. The CII portfolio underperformed the market at the same rate (approximately 5 times) when calculated over a one year or four year period.

Tables IV and V are also consistent with the change in the selection process over time by the Council of Institutional Investors. The Council reports that the selection criteria in 1993 weighed more heavily on stock performance than in prior years. In 1993 the benchmark portfolios outpaced the CII sample more consistently whether measured by short-term or long-run performance. The change in criteria is clearly seen in table V. Holding period returns for the 1991 and 1992 CII samples are indistinguishable from other firms in the same industry or the market as a whole.

4.2 Post Listing Performance

In this section we report our primary evidence consistent with the effectiveness of coordinated 'quiet' activism. Effective monitoring is expected to increase the value of the firm by pressuring management to act in the best interest of shareholders. The 'behind-the-scenes' nature of institutional monitoring makes it difficult to pinpoint a single event that represents a shift in management policy. Further, we do not expect to observe immediate action to meet or contact focus list firms. It may take several months before Council members react to release of the focus list. To avoid difficulties from attempting to date activism, we measure holding period returns for a full year after the Council's focus list is made public.

Table VI reports the stock market performance of firms on the Council lists relative to our benchmark firms in the following year. These returns are compounded daily starting from October 1 of each year until September 30 of the following year. Council listed firms significantly outperform all benchmark portfolios. For each sample year, these firms generated at least 10% higher returns than the S&P 500. Over the full sample, the CII portfolio exhibits a mean return of 21.1% in the year after listing (median of 19.4%) compared to the market return of 9.5% (median of 10.46%). This finding is consistent with the view that Council-listed firms were subject to substantial efforts to create shareholder value. Given that the mean equity market value of Council listed firms was $3.42 billion and that these 97 firms experienced a mean abnormal return of 11.6% we estimate a total abnormal dollar gain of these firms of $39.7 billion.

Comparing the CII sample with the risk-control portfolios yields similar inferences. In all comparisons, the median Council listed firm did significantly better than the benchmark portfolios. For example, the short-run market comparison group reports a median of holding period return of 2.8%, or almost seven times smaller than the CII sample. For all other comparison portfolios, the mean and the median returns are significantly greater for firms on Council's list. The mean one year stock market performance is 2 times greater than the long-term performance matched portfolio (5.3%) and 5 times greater than the book to market matched portfolio (2.2%).

Overall, there is substantial evidence that firms on Council of Institutional Investors focus lists far outperformed the market and reasonable comparison group firms in the 1991-93 period. This is consistent with the view that coordinated institutional shareholder activism is effective.

5.0 Operating Changes Following Appearance on Focus Lists

Table VII documents the frequency of changes in corporate operations and corporate governance before and after block share purchase for the 50 firms placed on the 1993 focus list. Among listed firms, there were very frequent programs of corporate divestitutes, layoofs and restructurings. This activity is consistent with the view that activism forced real change in these firms.

It is difficult to interpret the results in Table VII because a benchmark is not provided for a normal rate of divestiture. In Table VIII we provide a benchmark by computing changes in management activity after listing relative to the one year pre-listing period. The table shows that acquisition rates decline, divestiture rates go up signficantly and that top management change slows down (if anything). We interpret this as evidence that institutional activism gets some of its results by forcing change, but not necessarily by removing existing management. Despite well-publicized cases at American Express, Kodak, IBM and General Motors where activism was associated with a change in CEO, most firms on the 1993 CII focus list did not experience such a change.

6.0 Conclusion

In an effort to understand whether efforts at coordinating institutional shareholder activism through the Council of Institutional Investors are effective, we have investigated the performance of firms which appeared on focus lists distributed by the Council in 1991, 1992 and 1993. The Council has provided a forum for a large group of public and private pension funds to share information about a variety of matters including activism programs designed to accelerate solution of problems in underperforming firms.

As expected, this study finds that firms experienced deteriorating earnings and exhibit below average share price performance in the year before being included on a focus list. In the year after being listed, these firms experienced an average share price increase of 9% above the S&P 500. This improvement in holding period returns is robust for a variety of risk adjustments. Matching portfolios created on the basis of long- and short-term performance prior to inclusion on the focus list, book to market ratio prior to inclusion and industry earned significantly lower mean and median returns.

In order to broaden our understanding of the efficacy of coordinated institutional activism, we plan to look for observable indications that management is changing its course. Examples of these activities include, but are not limited to, divestitures, management turnover, corporate refocusing, and governance changes. We plan to tests for differences in the occurance of these events between Council focus list firms and firms in the matching portfolios. We also plan to test for differences in occurance in the CII sample prior to and after inclusion on the focus list.

The results of this study are broadly consistent with the view that coordinated institutional governance activism is effective. Our results contrast with those of some other recent studies which document little market response to proxy resolutions and activism campaigns. We attribute the difference in results to several factors. First, we focus on firms which were subject to coordinated activism rather than individual campaigns run by a single pension fund. Second, we only look at firms relative to when they appeared on a Council of Institutional Investors focus list. This allows us to focus on the effect of concerted monitoring that takes place out of public view. This sidesteps the potential problem with studies that focus primarily on public governance events (e.g. proxy proposals) that the most recalcitrant (and least likely to improve) firms are likely to be selected. It might very well be that management teams are most responsive to activism efforts which are private and done in the context of a long-term relationship.

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TABLE 1
SAMPLE DESCRIPTION

This table describes the number of firms on the Council of Institutional Investors focus lists in 1991, 1992 and 1993 along with the median market value of equity, stock exchange, index membership and firm age of these firms. Firm age is measured as the number of years listed on the CRSP tapes (maximum possible years: 68).

	No. of Firms	Mkt. Value of Equity	No. on NASDAQ	No. in S&P 500	Med. Years on CRSP
1991	16	4,148.46	1	15	39
1992	25	4,633.66	0	24	39
1993	56	2,325.13	4	41	31
Total	97	3,420.64	5	80	31

TABLE 2
DESCRIPTION OF COMPARISON GROUP FIRMS

Performance of firms on Council of Institutional Investors focus lists is compared to a variety of benchmark portfolios which adjust for market movements, potentially special risk characteristics or known anomalies. All firms in benchmark portfolios were listed on the New York Stock Exchange.

Benchmark Portfolio	Name	How Calculated	Controls For
Standard & Poors 500	S&P500	Use return on CRSP tape	Market movement, size effect (Banz 1981).
Short-run return match	SRM	Firms matched by stock return in the year before appearance on a focus list.	Short-run reversal (Zarowin 1991); Momentum effect (Jegadeesh and Titman (1993).
Long-run return match	LRM	Firms matched by stock return in the four years before appearance on a focus list.	Long-run reversal (DeBondt and Thaler (1987)).
Book to market	BTM	Firms matched by the book to market ratio in the period prior to appearance on a focus list	Distress risk effect (Fama and French (1990)).
Industry	IND	All NYSE firms that match on the primary four-digit SIC codefound on the Compustat PST tape.	

TABLE 3
OPERATING CASH FLOW PERFORMANCE OF FIRMS ON COUNCIL FOCUS LISTS

The mean and median operating cash flows[1] for the portfolio of CII focus list firms (CII), a portfoilo of firms matched to the CII focus list firms on stock performance in the year prior to selection (SRM), a portfolio matched on returns for the four years prior to selection (LRM), a portfolio matched on the book-to-market ratio for the fiscal year prior to selection (BTM), and the S & P 500 (S&P). Inter-sample diferences are noted as:* for the 10% level, ** for the 5% level and *** for the 1% level.

Panel A: Firms Selected by CII in1991

Year	**CII**	**SRM**	**LRM**	**BTM**	**S&P**
-3	0.222	0.191	0.251	0.181	0.204
	0.205	0.199	0.166	0.174	0.189
-2	0.225	0.208	0.362	0.156	0.189
	0.208	0.193	0.196	0.143*	0.174
-1	0.170	0.186	0.475	0.219	0.200
	0.199	0.181	0.208	0.196	0.188
0	0.162	0.170	0.324	0.143	0.167
	0.155	0.165	0.220	0.147	0.162
+1	0.150	0.160	0.263	0.182	0.168
	0.140	0.152	0.170	0.171	0.159

Panel B: Firms Selected by CII in1992

Year	**CII**	**SRM**	**LRM**	**BTM**	**S&P**
-3	0.220	0.176	0.200	0.206	0.189
	0.196	0.159	0.212	0.222	0.174
-2	0.178	0.208	0.218	0.245	0.200
	0.201	0.225	0.201	0.212	0.188
-1	0.178	0.146	0.169	0.194	0.167
	0.163	0.133	0.156	0.164	0.162
0	0.166	0.156	0.217	0.166	0.167
	0.148	0.161	0.180*	0.148	0.158

Panel C: Firms Selected by CII in1993

Year	**CII**	**SRM**	**LRM**	**BTM**	**S&P**
-3	0.209	0.197	0.180	0.157	0.196
	0.191	0.193	0.177**	0.208	0.188
-2	0.166	0.179	0.158	0.107	0.169
	0.170	0.158	0.146	0.182	0.166
-1	0.172	0.176	0.143**	0.158	0.166
	0.168	0.151	0.154**	0.163	0.156

[1] Operating cash flows are reported as earnings before interest, taxes and depreciation divided by the book value of assets.

TABLE 4
FOUR YEAR PRIOR SELECTION PERFORMANCE

The mean and median holding period returns for the portfolio of CII focus list firms (CII), a portfoilo of firms matched to the CII focus list firms on stock performance in the year prior to selection (SRM), a portfolio matched on returns for the four years prior to selection (LRM), a portfolio matched on the book-to-market ratio for the fiscal year prior to selection (BTM), and the S & P 500 (S&P). Inter-sample diferences are noted as:* for the 10% level, ** for the 5% level and *** for the 1% level.

Portfolio		1991	1992	1993	Total
CII	Mean	-18.17	44.07	3.55	10.34
	Median	-16.16	-5.82	-1.84	-6.18
	N	16	25	55	96
SRM	Mean	15.96***	44.19	11.56	20.70
	Median	7.73***	38.29*	19.91	21.09***
	N	16	25	55	96
LRM	Mean	-18.20	43.32	2.19	9.42
	Median	-16.17	-5.83	-1.91	-6.47
	N	16	25	55	96
BTM	Mean	-0.30	32.11	69.18***	47.72**
	Median	-9.69	23.26***	40.88***	24.09***
	N	16	25	55	96
IND	Mean	13.06**	42.08	44.34***	38.71***
	Median	1.04	21.43	24.31***	19.35***
	N	184	356	574	1,114
S&P	Mean	41.13**	76.40	55.70***	58.65***
	Median	26.34***	57.38***	41.14***	40.45***
	N	500	500	500	1,500

TABLE 5
ONE YEAR PRIOR SELECTION PERFORMANCE

The mean and median holding period percentage returns for the portfolio of Council of Institutional Investors focus list firms (CII), a portfolio of firms matched to the CII focus list firms on stock performance in the year prior to selection (SRM), a portfolio matched on returns for the four years prior to selection (LRM), a portfolio matched on the book-to-market ratio for the fiscal year prior to selection (BTM), and the S & P 500 (S&P). Inter-sample diferences are noted as:* for the 10% level, ** for the 5% level and *** for the 1% level.

Portfolio		1991	1992	1993	Total
CII	Mean	34.05	13.68	-7.11	4.91
	Median	26.03	4.06	-3.22	1.85
	N	16	25	56	96
SRM	Mean	34.09	13.38	-7.02	5.02
	Median	26.04	3.81	-2.84	1.96
	N	16	25	55	96
LRM	Mean	12.20**	33.91	20.93***	22.83***
	Median	17.23*	6.89	15.31***	13.65***
	N	16	25	55	96
BTM	Mean	24.24	-2.24	31.69***	21.46***
	Median	13.02	-5.44	24.37***	17.56***
	N	16	25	55	96
IND	Mean	44.98	11.67	21.57**	22.37**
	Median	40.62	6.67	14.29***	19.35**
	N	184	356	574	1,114
S&P	Mean	30.48	13.87	16.28***	17.31***
	Median	28.94	11.66	15.08***	15.11***
	N	500	500	500	1,500

TABLE 6
POST SELECTION PERFORMANCE

The mean and median holding period returns for the portfolio of CII focus list firms (CII), a portfoilo of firms matched to the CII focus list firms on stock performance in the year prior to selection (SRM), a portfolio matched on returns for the four years prior to selection (LRM), a portfolio matched on the book-to-market ratio for the fiscal year prior to selection (BTM), and the S & P 500 (S&P). Inter-sample diferences are noted as:* for the 10% level, ** for the 5% level and *** for the 1% level.

Portfolio		1991	1992	1993	Total
CII	Mean	24.52	33.58	15.91	21.10
	Median	19.52	25.92	14.96	19.40
	N	16	25	55	96
SRM	Mean	0.92*	9.45*	15.15	11.71
	Median	-4.78*	4.30*	3.04*	2.80***
	N	16	25	55	96
LRM	Mean	-0.02*	7.13**	6.40***	5.34***
	Median	-1.28*	14.29**	6.86**	7.45***
	N	16	25	55	96
BTM	Mean	12.44	-2.10***	1.53***	2.24***
	Median	15.85	9.02***	-2.53***	0.00***
	N	16	25	55	96
IND	Mean	20.31	29.77	7.99***	16.99***
	Median	16.77	24.03	1.62***	8.95***
	N	184	356	574	1,114
S&P	Mean	13.79	22.28	4.02***	9.51**
	Median	11.66	19.08	2.49***	10.46**
	N	500	500	500	1500

TABLE 7
MANAGEMENT ACTIVITY: 1993

The number of firms on the Council of Institutional Investors 1993 Focus List that engage in activities associated with management attempts to increase performance in the year after inclusion.

Activity	Number of firms
Restructuring	17
Refocusing	10
New strategy	4
Acquisition	20
Divestiture	29
Cost cutting	24
Layoffs	29
Cut investments	2
Cut dividends	18
Special dividend	1
Increase debt	5
Decrease debt	14
Change CEO	8
Change top manager	14
Issue equity	6
Stock repurchase	5

TABLE 8
PRE- AND POST-FOCUS LIST MANAGEMENT ACTIVITY: 1993

The number of firms engaging in activities associated with managment attempts to increase performance in the year prior to and the year after inclusion on the Council of Institutional Investors 1993 focus list.

Activity	**Prior**	**Post**	χ^2
Acquisition	26	20	0.92
Divestiture	20	29	2.32
Change CEO	16	8	0.88
Change top manager	19	14	1.07
Total	81	71	0.81

APPENDIX: LIST OF FIRMS ON THE COUNCIL OF INSTITUTIONAL INVESTORS LIST, 1991-93 AND STOCK RETURN IN THE YEAR AFTER LISTING.

Company	**Year**	**Stock Return in Year after Listing (percentage)**
Aetna Life	91	28.76
American Express	91	-10.67
Apple Computer	91	-7.97
Champion International	91	0.77
Chase Manhattan	91	30
Chrysler	91	138.8
Dial Corp.	91	38.9
Digital Equipment	91	-29.9
General Dynamics	91	87.1
IBM	91	-17.7
ITT	91	26.6
Sears	91	22
Time Warner	91	16.9
TJX Companies	91	36.3
Tribune Co	91	16.1
Woolworth	91	16.4
American Express	92	68.57
Boise Cascade	92	11.3
Caterpillar	92	55.03
Champion INTL	92	20.58
Chrysler	92	110.7
Citicorp	92	144
Coca-cola	92	5.95
Dial Corp.	92	3.78
Dow Chemical	92	9.18
Eastman Kodak	92	38.7
Federal Express	92	71.3
General Dynamics	92	80.1
IBM	92	-45.7
National Medical Enterprises	92	-14.4
Occidental Petroleum	92	23
Pennzoil	92	25.9
Sears	92	68.3
Tenneco	92	48.2
Time Warner	92	70.4
Travelers	92	77.2
Unisys	92	30.14
US Surgical	92	-66.4
W. R. Grace	92	-4.55
Westinghouse	92	-17.1
Whitman	92	21.12
Alcan Aluminum	93	43.45
ALCOA	93	28.96
Allergan	93	-15.7
Alza	93	-6.78
American Brands	93	18.17
American Cyanimid	93	95.4
Ball Corp	93	-3.21
Baxter International	93	31.55

BCE Inc	93	16.02
Bethlehem Steel	93	46.1
Black & Decker	93	9.56
Borden	93	-20.5
Bruno's	93	-15.39
Brunswick	93	46.78
CBI Industries	93	9.1
Cominco	93	65.91
Consolidated Freightways	93	38.58
Costco	93	-1.37
Cyprus Minerals	93	33.24
Dow Jones & Co	93	-7.66
Du Pont	93	28.81
Fina	93	14.95
Food Lion	93	1.5
Genzyme Corp	93	2.24
Goodrich	93	0.27
IBM	93	68.61
Intl Paper	93	33.39
Jostens	93	-4.96
K Mart Corp	93	-22.3
Knight-Ridder Inc	93	-2.45
Loews Corp	93	-2.37
Maytag Corp	93	24.57
Mercantile Stores	93	28.6
Midwest Resources	93	-22.17
National Medical Enterprises	93	77.92
Navistar	93	41.58
New York Times	93	-10.1
Northern Telecom	93	44.28
Pacificorp	93	-8.86
Pep Boys-Manny Moe	93	47.94
Price Co	93	-9.53
Reynolds Metals	93	38.83
Rite Aid Corp	93	37.17
RJR Nabisco Holdings	93	52.78
Safety-Kleen	93	9.81
Scott Paper	93	90.16
Scripps (E. W.)	93	15.39
Shoney's	93	-37.64
Student Loan Mktg	93	-24.69
Times Mirror	93	10.54
Timken	93	30.15
Triton Energy	93	3.17
Union Carbide	93	80.68
US Shoe Corp	93	116
US Surgical	93	28.47
USAIR Group	93	-63.37
Woolworth Corp	93	-28.86