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Hedge fund activism in family firms

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Abstract

Research Summary: This article examines the antecedents and outcomes of hedge fund activism in family versus nonfamily firms. We find that activist hedge funds are less likely to initiate campaigns against family firms than nonfamily firms, but the cumulative abnormal returns to announcements of campaigns against family firms exceed those of nonfamily firms. The presence of one or more family members on a firm's board of directors appears to be a key impediment to hedge fund activism in family firms. Additionally, activist hedge funds are more likely to use hostile tactics and demand more substantive changes in their campaigns against family firms than nonfamily firms. Together, these findings contribute to the agency theory-based literatures on hedge fund activism, family firms, boards of directors, and corporate governance.

Managerial Summary: Activist hedge funds are a significant force in corporate governance, driving the companies they target to change their strategies, structures, and leadership. Family firms are prevalent and economically important, accounting for a third to a half of companies worldwide. This article compares hedge fund activism in family versus nonfamily firms. Activist hedge funds are about 41% less likely to initiate campaigns against family than nonfamily firms, but the average returns to successful activist hedge fund campaigns against family firms are about 2% higher than in nonfamily firms. These effects are especially pronounced when family members serve on

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a company's board of directors. Furthermore, activist hedge funds are more likely to use hostile tactics and demand more substantive changes in campaigns against family than nonfamily firms.

KEYWORDS

activist hedge funds, boards of directors, corporate governance, family firms, hedge fund activism

1 | INTRODUCTION

Activist hedge funds have become powerful actors in corporate governance, impelling major strategic changes in companies all around the world. Between 2015 and 2021, activist hedge funds initiated nearly 4000 campaigns against US public companies (Activist Insight, 2021), achieving their demands in more than a third of these campaigns (Activist Investor Report, 2020). The growing importance of hedge fund activism has led to a concomitant increase in interest from strategic management researchers (Ahn & Wiersema, 2021; Goranova & Ryan, 2014), who have examined both the antecedents (DesJardine et al., 2021; DesJardine & Shi, 2023; DesJardine, Shi, & Marti, 2023) and outcomes (Brauer et al., 2023; Chen et al., 2021; Chen & Feldman, 2018; DesJardine et al., 2022; DesJardine & Durand, 2020; Shi et al., 2021; Wiersema et al., 2020) of this phenomenon. This body of research is especially important when viewed against the broader backdrop of research on corporate governance (e.g., Connelly et al., 2010; DesJardine, Zhang, & Shi, 2023; Misangyi & Acharya, 2014; Shi et al., 2017).

Alongside this research, a large body of agency theory-based literature has explored how the board, ownership, and control structures of family firms influence their decisions, performance, and stock market valuations (Anderson & Reeb, 2003, 2004; Feldman et al., 2016, 2019; Villalonga et al., 2015; Villalonga & Amit, 2006, 2020). Family firms are widely prevalent and economically important, accounting for anywhere from a third to a half of public and private companies in the United States and around the world (Claessens et al., 2000; Faccio & Lang, 2002; La Porta et al., 1999; Villalonga & Amit, 2009, 2010). Family firms are prone to make suboptimal decisions from the perspective of maximizing value for nonfamily shareholders, making them attractive candidates for hedge fund activism. However, family firms' board, ownership, and control structures may insulate them from having to rectify performance and governance shortcomings in the manner that hedge fund activists demand (Kastiel, 2016). Thus, family firms provide an ideal context in which to investigate this article's research questions: what are the antecedents and outcomes of hedge fund activism against family firms versus nonfamily firms?

We theorize that activist hedge funds are less likely to initiate campaigns against family firms because these firms' board, ownership, and control structures make it harder and more costly for activist hedge funds to do so—in other words, family firms are worse opportunities (DesJardine, Shi, & Marti, 2023) for hedge fund activism than nonfamily firms.[1] At the same time, because it is more costly to initiate campaigns against family firms, activist hedge funds

[1]One commentator nicely reflected this point in his assessment of Nelson Peltz's chances of success in Trian Fund Management's 2020 campaign against Comcast Corporation, a family firm whose CEO (and the son of the founder), Brian Roberts, serves on the board of directors and controls a 33% voting share: "Unless there's a shareholder mutiny at an enormous scale—highly unlikely—Roberts can simply tell Peltz to kick rocks" (Sherman, 2020).

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will only do so when the problems in these companies are so severe that the expected returns to campaigns against them exceed the returns to campaigns against nonfamily firms. Because investors share in the expected upside to activist hedge fund campaigns without incurring any of the costs (Gantchev, 2013), they should react more favorably to announcements of activist hedge fund campaigns against family than nonfamily firms, resulting in higher cumulative abnormal returns (CAR) to the former than the latter.

Using hand-collected data on a sample of 5100 firm-year observations pertaining to 631 unique public companies from 2010 to 2018, we find support for these arguments. Initially defining family firms as those in which a firm's founder or a member of his/her family by blood or marriage is an officer, director, or blockholder (Anderson & Reeb, 2003; Villalonga & Amit, 2006, 2009, 2010), we find that activist hedge funds are about 41% less likely to initiate campaigns against family firms than nonfamily firms, but the returns to announcements of activist hedge fund campaigns against family firms are about 2% higher than in nonfamily firms. We conduct an extensive set of post hoc analyses to explore the mechanisms behind and robustness of these baseline findings. Most importantly, we establish that the presence of one or more family members on a firm's board of directors (but not as a large shareholder or voteholder) is a key impediment to hedge fund activism in family firms. This analysis helps disentangle the different mechanisms—board versus ownership and control structures—that may insulate family firms from hedge fund activism. We also document that activist hedge funds are more likely to use hostile (and hence, costlier) tactics and to demand more substantive changes in their campaigns against family firms than nonfamily firms. Finally, we establish that our results are robust to different definitions of nonfamily firms, and to the use of propensity score matching (PSM) models to mitigate the possibility of bias from selection on observable characteristics (DesJardine & Durand, 2020).

2 | THEORY AND HYPOTHESES

2.1 | Hedge fund activism: Problems and opportunities

Which firms do activist hedge funds target? The traditional view is that activist hedge funds proactively accumulate concentrated ownership stakes in and initiate campaigns against firms that have problems (Ahn & Wiersema, 2021; Brav et al., 2008; Goranova & Ryan, 2014). Stock market undervaluation and underperformance relative to peers are prominent concerns that tend to attract activist hedge funds, though there are a host of other characteristics (many of which are correlated with undervaluation and underperformance) that do so as well: slowing growth in core markets, underinvestment in capital initiatives, excessive diversification, governance problems such as CEO duality or board busyness, corporate social responsibility signals, goodwill impairment, excessive leverage, low credit quality, and even displays of agentic values by CEOs (Boyson & Mooradian, 2011; Clifford, 2008; Denes et al., 2017; DesJardine et al., 2021; DesJardine & Shi, 2023; DesJardine, Shi, & Marti, 2023; Klein & Zur, 2009). Activist hedge funds are highly motivated to maximize economic value in the firms they target, which they do by holding managers accountable for their actions and pressuring them to address various performance and governance shortcomings (DesJardine & Durand, 2020). The improvements that activist hedge funds demand usually seek to address the above-described problems. These demands typically manifest themselves along three, nonmutually exclusive dimensions: corporate scope, operational efficiency, and corporate governance.

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Activist hedge fund demands to change corporate scope usually entail divestitures of non-core businesses or perhaps even the sale of the entire company. About one quarter of activist hedge fund campaigns annually demand that firms divest some of or all their operations (Lazard, 2021), and activist-impelled divestitures have been shown to outperform divestitures that managers undertake of their own accord both in the short- and the long-term (Chen & Feldman, 2018). Beyond divestitures, activist hedge funds' scope-related demands also involve changes to how financial capital is used and deployed, such as blocking M&A transactions, curtailing certain strategic investments, returning cash to shareholders, or improving the firm's capital structure (e.g., DesJardine et al., 2022; Leute et al., 2023).

Activist hedge fund demands to enhance operational efficiency involve strategic plans to reduce costs or to increase revenue growth, as well as to cut excessive executive compensation. One famous example of a campaign involving operational demands was Starboard Value's 2014 campaign against Darden Restaurants seeking to improve operating performance, particularly at the Olive Garden restaurant chain. Starboard identified numerous—and quite granular—areas for potential operational improvements in these restaurants, including streamlining kitchen operations, increasing alcohol sales, and cutting down on food waste.

Finally, corporate governance demands typically address the composition of the board of directors (usually, the replacement of certain directors with representatives of the activist hedge fund) or the ouster of underperforming management teams. Corporate governance demands, especially around directorships, often lead to the implementation of corporate portfolio and operational efficiency demands, since a seat on the board of directors is often a primary vehicle through which activist hedge funds become able to effectuate other changes. Thus, demanding board seats is one of the most frequently used tactics by activist hedge funds, who gained more than 1500 board seats in US public companies between 2015 and 2021 (Activist Insight, 2021).

Recent research has begun to explore the possibility that in addition to problems, corporate opportunity structures, defined as the features of firms that make them more (or less) attractive to activists (e.g., Briscoe et al., 2014), may also be an important determinant of the likelihood of hedge fund activism. This research suggests that problems and opportunities may interact to shape the propensity of activist hedge funds to target certain firms (DesJardine, Shi, & Marti, 2023). In other words, conditional on having problems that activist hedge funds might seek to redress, certain firms may provide better opportunities for hedge fund activism, especially when activist hedge funds "assume that certain attributes of a firm—such as its size or board composition—increase the likelihood that they can successfully influence a firm" (DesJardine, Shi, & Marti, 2023, p. 2). Accordingly, activist hedge funds may be more likely to initiate campaigns against firms that have problems when there are also greater opportunities to exert influence.

2.2 | Likelihood of hedge fund activism in family versus nonfamily firms

These insights about the interaction between problems and opportunities in shaping the likelihood of hedge fund activism provide a useful lens through which to compare the relative propensity of activist hedge funds to initiate campaigns against family versus nonfamily firms. Consistent with the notion of corporate opportunity structures, certain characteristics of firms' board, ownership, and control structures may make them better opportunities for hedge fund

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activism, since these attributes reflect two avenues through which activist hedge funds may be able to exert influence.

First, activist hedge funds frequently seek board seats in the firms they target, to be able to direct decision-making from within the organization. In so doing, activist hedge funds may be better able to monitor managers and shape their strategic and financial decision-making. Thus, firms in which it is easier to attain board seats may be better opportunities for hedge fund activism. Per this point, DesJardine, Shi, and Marti's (2023) main finding is that firms with more demographically diverse boards may be better opportunities for hedge fund activism, since this characteristic makes these firms slower and less united in responding to it. Second, activist hedge funds can leverage their voting power to ensure that their demands are implemented. Many important decisions, such as changes to the articles of incorporation, M&A, and various changes to governance provisions, may require a shareholder vote. Activist hedge funds can vote their shares in favor of changes they wish to see made, and they can galvanize other shareholders to do the same (Ahn & Wiersema, 2021). Thus, firms whose ownership and control structures make it easier to attain voting power may also be more attractive opportunities for hedge fund activism (Kastiel, 2016).

Family and nonfamily firms have different board, ownership, and control structures, influencing the extent to which they are attractive opportunities for hedge fund activism. In terms of board composition, most directors in nonfamily firms are independent and rarely hold large ownership stakes (Anderson & Reeb, 2004). Although independent directors are not always effective (Feldman & Montgomery, 2015; Hambrick & Jackson, 2000), they are elected annually and can only be removed through a fair voting process. In nonfamily firms, this may enable activist hedge funds to replace incumbent directors with their own representatives.

In contrast, families often enjoy disproportionate board representation, which may allow them to elect a share of the board that exceeds their economic ownership (Villalonga & Amit, 2009). Family owners often place family members or their close associates in important board positions, enabling them to influence (if not control) the firm's management, strategic direction, and voting agenda (Anderson & Reeb, 2004; Villalonga & Amit, 2009). Family-affiliated board members could be more difficult to remove in elections, since they might be supported by the concentrated votes of family owners and may, themselves, be large shareholders. The fact that fewer board seats are available could make it harder for activist hedge funds to place their own nominees on these boards (Kastiel, 2016). Even if activist hedge funds succeed in electing their own representatives, they might still need to win over the incumbent family directors to gain control of it, further limiting activist hedge funds' ability to direct decision-making.

In terms of ownership and control structures, in nonfamily firms, insiders rarely hold a superior class of shares (Gompers et al., 2010), which should enable activist hedge funds to accumulate ownership in these firms relatively quickly and inexpensively. Activist hedge funds' ownership stakes can enable them to place their demands on proxy ballots and to swing the vote in their favor (Ahn & Wiersema, 2021). Additionally, nonfamily firms usually have a significant passive institutional investor presence (Fichtner et al., 2017). Due to their large holdings, these investors are incentivized to support initiatives that may increase a firm's share price (Appel et al., 2019; Brav et al., 2008). This should enable activist hedge funds to rally shareholder support behind their causes.

In contrast, not only might family members be large shareholders in their firms, but they may also hold voting rights in excess of their shareholdings through dual-class shares, pyramids, crossholdings, or voting agreements (La Porta et al., 1999; Villalonga & Amit, 2009). For instance, dual class shares with super-voting rights allow family owners to exercise control over any decision that requires a shareholder vote. Since these shares are rarely accessible to

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investors in the open market, activist hedge funds may be at a profound disadvantage when contesting family owners (Kastiel, 2016).[2] Additionally, some family owners enter into voting agreements with other large shareholders to form coalitions (Villalonga & Amit, 2009). These shareholders have the right to cede their voting power to family owners, allowing the family owners to vote on their behalf (Bennedsen & Wolfenzon, 2000; Morck et al., 2005). This may make it harder for activist hedge funds to rally support from other shareholders.

The foregoing discussion indicates that the board, ownership, and control structures of family firms may make them worse opportunities for hedge fund activism than nonfamily firms, leading to differences in the relative likelihood of activist hedge fund campaigns against these two types of firms. Specifically, family owners' control over their firms' boards of directors and their superior voting rights should limit the formal channels through which activist hedge funds might gain a foothold (Kastiel, 2016). This should make family firms worse opportunities for hedge fund activism than nonfamily firms, even if the problems that warrant hedge fund activism in the first place are similar.

> **Hypothesis 1.** Ceteris paribus, activist hedge funds are less likely to initiate campaigns against family firms than nonfamily firms.

2.3 | Returns to hedge fund activism in family versus nonfamily firms

Having predicted that activist hedge funds are less likely to initiate campaigns against family firms than nonfamily firms, it is important to recognize that they still do so. This indicates that it may be worthwhile for activist hedge funds to initiate campaigns against family firms when the expected benefits outweigh the costs. Because the costs of hedge fund activism against family firms are likely to be higher than nonfamily firms, so must their expected benefits for these campaigns even to occur. This has implications for investors' reactions, and hence, shareholder returns to announcements of activist hedge fund campaigns against family and nonfamily firms.

2.3.1 | Costs of hedge fund activism

Initiating an activist hedge fund campaign against any public company is expensive. As Gantchev (2013, p. 611) puts it, "In addition to unobservable costs such as the time and effort of negotiating with a target, an activist bears disclosure, legal and other fees of hiring proxy advisors, corporate governance experts, investment banks, public relations, and advertising firms." Gantchev (2013) estimates the costs of three tactics activist hedge funds use in their campaigns, finding that the average costs of demand negotiations, seeking board representation, and proxy fights are $2.94 million, $1.83 million, and $5.94 million, respectively.[3]

[2]In Comcast, for example, the Roberts family owns less than 3% of the equity in the company, but it controls 33.33% of the votes through its ownership of 100% of the Class B super-voting shares, which are not publicly traded.

[3]This is consistent with Carl Icahn's experiences in getting his nominees appointed to boards of directors: "...typically even a large shareholder must conduct an expensive proxy contest to elect its nominees—that is, he needs to solicit enough votes from other shareholders. This is accomplished by mailing a statement describing the shareholder's positions, and a card on which to vote. At a large public company, mailing, printing, and other costs can run into the millions of dollars" (Icahn, 2009).

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Because family firms' distinct board, ownership, and control structures make them worse opportunities for hedge fund activism, activist hedge funds are likely to need to use more hostile tactics in their campaigns against family firms than nonfamily firms, suggesting that the costs of campaigns against family firms will exceed nonfamily firms. Insulated by family control over their firms' boards and/or voting shares, family firms may feel less threatened by initial demand letters or phone calls from activist hedge funds, and thus, less likely to settle with them upfront (Kastiel, 2016). To have their demands met in family firms, activist hedge funds may therefore need to resort to more confrontational tactics such as proxy contests and lawsuits that incur advertising expenses, charges related to regulatory filings, proxy distribution costs, and fees payable to various proxy and legal advisors. The use of more confrontational tactics also implies that activist hedge funds may have to commit to longer timelines in campaigns against family firms, as lawsuits and proxy contests take longer to settle than informal negotiations (Gantchev, 2013). This could create opportunity costs, as activist hedge funds may not be able to easily liquidate their stakes to invest in other targets.

2.3.2 | Expected benefits of hedge fund activism

The expected benefits of activist hedge fund campaigns that are initiated against family firms should, in turn, exceed those of nonfamily firms. As DesJardine et al. (2023, p. 19) aptly point out, "the size of the problems that a firm exhibits and the opportunities activists have to influence the firm have a multiplicative effect, in which problems determine the *size* of the potential payout for activist hedge funds, whereas opportunities determine the *likelihood* of the potential payout." Family firms are worse opportunities for hedge fund activism than nonfamily firms due to the impediments created by their board, ownership, and control structures. Following DesJardine, Shi, and Marti's (2023) logic, this suggests that the *likelihood* of a payout from activist hedge fund campaigns against family firms should be lower than nonfamily firms. Accordingly, for it to be worthwhile for the activist hedge fund to expend the cost of initiating a campaign against a family firm, the problems in that company must be so severe that the *size* of the payout exceeds that of the average campaign against a nonfamily firm.

The problems that prompt hedge fund activism in family firms are likely to be more severe than in nonfamily firms. Activist hedge funds initiate campaigns against firms making suboptimal decisions such as excessive diversification, underinvestment in productive opportunities, inefficient operational processes, and subpar governance practices (Boyson & Mooradian, 2011; Clifford, 2008; Denes et al., 2017; DesJardine et al., 2021; DesJardine & Shi, 2023; Klein & Zur, 2009), many of which family firms are more likely to make than nonfamily firms.

For instance, because a family's economic well-being is often tied to the performance of a single business enterprise, family firms are more likely to diversify into unrelated domains when business risk increases and when performance declines (Gómez-Mejía et al., 2010), or simply because they "prefer to enter new businesses about which [they know] little but that are alluring personally" (Gilson, 2005, p. 1667). A famous example of this exact tendency is the case of Kohler, a family firm that diversified into hospitality and golf courses in the face of intensifying competition in its core plumbing fixtures business (Villalonga & Amit, 2008). Relatedly, family firms are less likely to divest than comparable nonfamily firms, even though divestitures often create shareholder value and operational improvements (Feldman et al., 2016). For example, it took pressure from two activist hedge funds and a major shareholder over multiple years

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to get The New York Times Company to divest non-core assets such as its stakes in the Boston Red Sox, Roush Fenway Racing, and *The Boston Globe* newspaper, among others (Kastiel, 2016). Finally, family firms often pursue suboptimal governance practices such as maintaining dual class share structures (La Porta et al., 1999; Villalonga & Amit, 2009) or creating employment opportunities for family members (Anderson et al., 2009; Villalonga & Amit, 2006). These practices may entrench and isolate family members from market discipline (Kastiel, 2016), or elevate less competent family members into leadership roles ahead of more qualified outsiders (Bennedsen et al., 2007; Calabrò et al., 2018; Pérez-González, 2006).

The expected returns to activist hedge fund campaigns that seek to mitigate these and other types of problems are often significant (e.g., Brav et al., 2008; Brav et al., 2018; Chen & Feldman, 2018; Clifford, 2008),[4] consistent with the fact that activist hedge funds "generally seek to improve the targeted firm's stock price so they can sell their shares at a profit" (DesJardine & Durand, 2020, p. 1057). Thus, because the problems that prompt hedge fund activism may be more severe in family firms than nonfamily firms, the expected returns to activist hedge fund campaigns that are initiated against family firms—the size of the payout the activist hedge fund receives—should be higher than the expected returns to the average campaign against a nonfamily firm.

2.3.3 | Investors' reactions to announcements of hedge fund activism

One of the unique features of hedge fund activism is that although the activist hedge fund bears the entire cost of initiating and executing a campaign against a particular firm, the returns from that campaign accrue to the firm's entire investor base, including the activist hedge fund (Appel et al., 2019; Grossman & Hart, 1980). Thus, investors enjoy the expected upside of the returns to activist hedge fund campaigns without incurring any of the costs (Gantchev, 2013). The use of more hostile tactics against family firms may portend to investors the higher returns that are expected to result from the mitigation of the (more severe) problems in these companies, as these returns must exceed the costs of activist hedge funds employing these more hostile tactics. This suggests that investors should react more favorably—translating into higher CAR—to the announcement of activist hedge fund campaigns against family firms than nonfamily firms.

> **Hypothesis 2.** Investors will react more favorably to announcements of activist hedge fund campaigns against family firms than nonfamily firms.

3 | METHODS

3.1 | Sample and data

To construct the sample, we first identified all firms that were listed in the Fortune 500 index in each year from 2010 to 2018, inclusive. We collapsed these lists into a single list of the 706 unique firms that ever appeared in the Fortune 500 index during this period, dropping 75 firms that were

[4]Despite these benefits, it is important to acknowledge that not all outcomes of hedge fund activism are favorable: for example, DesJardine and Durand (2020) find that corporate social performance is suppressed after activist hedge fund campaigns; Chen et al. (2021) show that hedge fund activism leads to the unwanted loss of human capital; and Shi et al. (2021) find that the incidence of workplace injury increases after institutional investor activism.

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not publicly traded. Then, we built a panel of firm-year observations out of this cross-section, resulting in a final sample of 5100 firm-year observations pertaining to 631 firms.

Because family ownership, control, and management vary over time, we next needed to determine which firm-year observations pertained to family versus nonfamily firms. We initially define family firms as those in which a firm's founder or a member of his/her family by blood or marriage is an officer, director, or blockholder (Anderson & Reeb, 2003; Villalonga & Amit, 2006, 2009, 2010), though we later vary the definition of this construct to elucidate the core mechanisms that may be driving our results. We gathered data on the identity of each firm's founder(s) or founding family from company websites, obituaries, Wikipedia, and other Internet searches. Subsequently, we reviewed each firm's annual proxy statements filed with the Securities and Exchange Commission (SEC) to determine if any family member related to the founder was listed as an insider (officer or director) and/or as a blockholder. If so, we manually gathered data on the family's leadership roles, ownership, and control structure from these proxy statements.

We then used SharkWatch to determine whether activist hedge funds initiated campaigns against the firms in our sample in any given year. SharkWatch is FactSet's corporate activism database, which compiles activist campaign data from company filings, press releases, dissident filings, financial news, company websites, and financial trade publications. We collected data on activist hedge fund campaigns that were announced between January 1, 2010 and December 31, 2018, but we excluded campaigns that only included "social/environmental or political" demands,[5] as well as those that were initiated by pension funds, ex-directors, and unions. Overall, 635 activist hedge fund campaigns were initiated against 250 Fortune 500 firms. We cross-checked the campaign data against other sources, such as Activist Insight Report, the *Wall Street Journal*, and corporate websites. Finally, we matched the list of activist hedge fund campaigns to our firm-year panel of Fortune 500 firms. While activist hedge funds initiated campaigns against more than half of the nonfamily firms in our sample at any point during the sample period, they only initiated campaigns against one-third of the family firms, consistent with Hypothesis 1.

Finally, we gathered data for our control variables from numerous sources: Compustat, CRSP, SDC Platinum, Thomson Reuters, Institutional Shareholder Services, ExecuComp, and BoardEx. We hand-collected missing data (especially on share structures, voting rights, board characteristics, ownership, and executive compensation) from SEC filings. To conserve space, we describe all our control variables in Appendix A1.

3.2 | Key variables

3.2.1 | Dependent variables

Hypothesis 1 predicts that activist hedge funds are less likely to initiate campaigns against family firms than nonfamily firms. As such, *Activist Targeted* takes the value one if an activist hedge fund initiated a campaign against a firm in a given year, and zero otherwise.

Hypothesis 2 predicts that investors will react more favorably to announcements of activist hedge fund campaigns against family firms than nonfamily firms. Announcement returns are measured using an event study in which we calculate *CAR*. *CAR* is the cumulative sum of

[5]Twenty three campaigns included social, environmental, or political demands in addition to the economic demands that are the primary focus of this study. We elected to keep these 23 campaigns in our sample because they still involved economic demands, though our results are unchanged if we eliminate these observations.

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abnormal returns during an event window surrounding the announcement of a particular event (in our case, the announcement of an activist hedge fund campaign). Abnormal returns are the difference between a firm's expected and actual returns during the event window, where expected returns are predicted based on the firm's and the stock market's returns during an estimation window that occurred well prior to the event window.[6] Following Chen and Feldman (2018), we calculated *CAR* using 250-day estimation windows ([−800, −551]) before the announcement dates of the activist hedge fund campaigns in our sample, and 3-day event windows ([−1, +1]) surrounding these announcement dates.[7]

3.2.2 | Primary independent variable

Our primary independent variable is *Family Firm*, defined as those firms in which the founder, the founder's descendant, or other family member by blood or marriage is listed in that year's proxy as an officer, director and or as a blockholder (with beneficial ownership rights exceeding 5%), either individually or as a group. This definition is consistent with prior studies that investigated family ownership and control among large, publicly traded US firms (Anderson & Reeb, 2003; Feldman et al., 2016; Villalonga & Amit, 2006, 2009, 2010). However, as mentioned previously, we also consider different definitions of *Family Firm* later in the paper to explore the potential mechanisms behind our results.

3.3 | Empirical methodology

To compare the likelihood of activist hedge fund campaigns against family versus nonfamily firms (Hypothesis 1), we run logistic regressions at the firm-year level. Buts, in any given year, there could be multiple campaigns initiated against certain firms. Thus, to compare the announcement returns of activist hedge fund campaigns against family versus nonfamily firms (Hypothesis 2), we run ordinary least squares regressions at the campaign-level. All regressions include the control variables described in Appendix A1, as well as two-digit SIC code and year fixed effects. Robust standard errors are clustered by firm. Summary statistics and correlation matrices at the firm-year and campaign levels appear in Appendix Tables A2 and A3.

4 | RESULTS

4.1 | Baseline regressions

Table 1 presents the results of baseline regressions testing Hypotheses 1 and 2. In Model [1], whose dependent variable is *Activist Targeted*, the coefficient on *Family Firm* is −0.527

[6]To test whether our results were affected by confounding events, we identified other major corporate events (such as dividend changes, stock splits, earnings announcements, stock repurchase programs, acquisitions, and major executive appointments) that may have been announced around the same time as activist hedge fund campaigns. We identified these events by searching through press release archives and announcements in major news sources. Results in which we excluded 60 confounded observations are consistent with the main results presented later in the paper.

[7]We tested the robustness of our results to alternate estimation ([−250, −51]) and event windows ([−1, 0], [0, +1], [−2, +2], [−3, +3]), and the results are consistent with our main findings.

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TABLE 1 Baseline results.

Dependent variables	[1] Activist Targeted	[2] CAR
Family firm	−0.527 (.006)	0.020 (.025)
ln(total sales)	0.364 (.000)	−0.003 (.392)
Tobin's *q*	−0.038 (.638)	0.005 (.206)
Return on assets	−3.932 (.005)	−0.029 (.457)
Capital intensity	6.291 (.000)	−0.073 (.155)
Leverage	1.519 (.001)	0.001 (.962)
Interest coverage ratio	0.003 (.006)	0.000 (.534)
Cash ratio	1.471 (.011)	0.007 (.791)
Firm age	0.001 (.828)	0.000 (.639)
Unrelated diversification	−0.724 (.066)	0.027 (.084)
Acquisition intensity	−0.014 (.451)	−0.001 (.029)
Firm growth	−0.220 (.642)	−0.014 (.365)
CEO turnover	0.082 (.562)	0.012 (.084)
CEO duality	0.031 (.838)	0.005 (.466)
CEO age	0.013 (.312)	0.000 (.618)
CEO incentive compensation	−1.247 (.006)	−0.009 (.537)
CEO stockholding	0.027 (.090)	−0.001 (.157)
Board size	0.086 (.041)	0.002 (.209)
Board ownership	1.319 (.011)	−0.045 (.031)
Average board tenure	0.016 (.567)	0.000 (.715)
Average board experience	−0.015 (.586)	0.001 (.480)
Total institutional ownership	−0.228 (.608)	−0.008 (.793)
Dual class share	−0.639 (.200)	−0.009 (.598)
Ownership-vote wedge	0.793 (.199)	0.008 (.667)
G-index	−0.007 (.917)	0.001 (.675)
Firm transparency	1.934 (.000)	0.049 (.004)
Analyst coverage	0.030 (.003)	0.000 (.688)
Analyst forecast accuracy	−0.648 (.002)	0.009 (.764)
Industry concentration	−0.243 (.544)	−0.012 (.554)
Industry sales growth	0.016 (.001)	0.000 (.181)
Constant	−9.072 (.000)	−0.022 (.714)
Year fixed effects	Yes	Yes
Industry fixed effects	Yes	Yes
Level of analysis	Firm-year level	Campaign-level
Specification	Logistic	OLS
Pseudo-R^2/R^2	.124	.103
Number of observations	3500	445
Robust standard errors are clustered by firm		
p-Values are in parentheses		

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($p = .006$), representing the log-odds ratio of activist hedge fund campaigns being initiated against family firms relative to nonfamily firms. Transforming this to an odds ratio, activist hedge funds are about 41% less likely to initiate campaigns against family firms than nonfamily firms, supporting Hypothesis 1. In Model [2], whose dependent variable is *CAR*, the coefficient on *Family Firm* is 0.020 ($p = .025$). This indicates that the announcement returns to activist hedge fund campaigns against family firms exceed those of nonfamily firms by 2.0%, supporting Hypothesis 2.

4.2 | Mechanism tests

4.2.1 | Definition of family firms

We argued that activist hedge funds may be less likely to initiate campaigns against family firms than nonfamily firms due to (a) the composition of family firm boards of directors, which may make it difficult for activist hedge funds to attain board seats in these companies, and (b) the ownership and control structures of family firms, which may make it difficult for activist hedge funds to accumulate shares in these companies and/or to generate support from other shareholders for their demands. Initially, we defined family firms as those in which a firm's founder or a member of his/her family by blood or marriage is an officer, director, or blockholder (Anderson & Reeb, 2003; Villalonga & Amit, 2006, 2009, 2010). Although this definition is well-established in the received literature, it lumps together the three different ways in which family members may exert influence in their firms: in management roles, on boards of directors, and/or as blockholders. Thus, by unpacking our existing definition of *Family Firm*, we have the unique opportunity to elucidate how family members may exert control in their companies and to identify which of their roles may impede hedge fund activism.

Table 2 presents the coefficients on *Family Firm* in regressions taking *Activist Targeted* and *CAR* as the dependent variables in Columns [1] and [2], respectively. In this table, *Family Firm* is defined in 15 different ways. Initially, we disaggregate the definition of *Family Firm* into its three component pieces: family firms are those in which one or more family members are (a) directors (Row D), (b) blockholders (Row B), or (c) officers (Row O). Next, we delve deeper into the management structure of family firms by defining them according to whether they are led by (d) family CEOs (Row CEO), (e) founder CEOs (Row FCEO), or (f) descendant CEOs (Row DCEO). Finally, we consider Villalonga and Amit's (2006) nine definitions of family firms (Rows 1–9), which enable us to examine more specific facets of family firm ownership (e.g., the family is the largest voteholder, the family is the largest shareholder and has at least 20% of votes, etc.) and/or to recombine aspects of the family's role in management, on the board, or as blockholders.[8]

Across all the different definitions of *Family Firm*, activist hedge funds remain less likely to initiate campaigns against family firms (Column [1]) when these companies are identified using definitions that contemplate one or more family members serving on their firm's board of

[8]Clearly, certain of these definitions are subsets of others; for example, the definition of family firms in Row 2 (at least one family officer and one family director) is a subset of the definition of family firms in Row D (one or more family members are directors). To clarify the overlap of treatment observations among the various definitions of family firms in this table, we include the number of treatment and control observations at both the firm-year-level and the campaign-level below each definition of family firms.

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directors (Rows D, 1, 2, 5, 6, 8, and 9). Transforming coefficient estimates into odds ratios, for example, Row D indicates that activist hedge funds are about 36% less likely to initiate campaigns against family firms, defined as those where one or more family members serves on the board of directors, than against nonfamily firms; Row 8 indicates that activist hedge funds are about 38% less likely to initiate campaigns against family firms, defined as those where one or more family members are directors or blockholders but there are no family officers, than against nonfamily firms. Among the remaining definitions of *Family Firm*, where no family member serves on the board of directors (Rows B, O, CEO, FCEO, DCEO, 3, 4, and 7), there is no difference in the likelihood of hedge fund activism between family and nonfamily firms. We observe a similar pattern for the CAR to announcements of activist hedge fund campaigns (Column [2]): the returns to announcements of campaigns against family firms exceed those of nonfamily firms only when the definition of *Family Firm* contemplates one or more family members serving on the board of directors (Rows D, 1, 2, 5, 6, and 8).[9]

These results support our argument that family board members are a key impediment to hedge fund activism. Family directors may make it difficult for activist hedge funds to attain board seats, normally a main vehicle through which to effectuate demands, limiting the likelihood of activist hedge fund campaigns against these firms. However, the presence of family members in firms' ownership and control structures does not impede hedge fund activism in the same way, as there is no difference in the likelihood of activist hedge fund campaigns against family versus nonfamily firms when the definition of *Family Firm* contemplates family members as large shareholders or voteholders. Board seats may be a more significant obstacle to hedge fund activism than ownership and control structures because a family's control over the board may prevent problems from even making it to shareholders for assessment (and potentially, resolution).[10]

Further interrogating our argument that the mechanism driving our results is the presence of family members on their firms' boards of directors and not in their ownership and control structures, Table 3 specifically considers definitions of family firms in which one or more family members are on these firms' boards of directors *and* there are also limits to the ownership and control that families have in/over these firms. As in Table 2, Table 3 presents the coefficients on these new definitions of *Family Firm* in regressions taking *Activist Targeted* and *CAR* as the dependent variables in Columns [1] and [2], respectively. We define family firms as those in which one or more family members serves on the board of directors *and* the family owns less than 1, 5, or 10% of the firm's total shares outstanding (Rows D-O1, D-O5, and D-O10), and as those in which one or more family members serves on the board of directors *and* the family controls less than 20 or 33% of the firm's total votes (Rows D-V20 and D-V33). Under all these definitions, activist hedge funds remain less likely to initiate campaigns against family firms than nonfamily firms, and the returns to announcements of activist hedge fund campaigns against family firms exceed those of nonfamily firms. These findings bolster our argument that the presence of family members on a family firm's board of directors, not in their ownership

[9]Although the definition of family firms in Row 9 does contemplate family members serving on the board of directors, the restrictiveness of the other components of this definition reduces the number of firm-year-level and campaign-level observations that are classified as family firms, weakening these results (especially in Column [2]).

[10]Using a count of the number of family directors as the key independent variable in these regressions indicates that activist hedge funds are about 20% less likely to initiate campaigns against family firms for each additional family director on their boards. This result lends support to the possibility that groups or coalitions of family members may make it even harder for activist hedge funds to gain control and/or influence decision-making in family firms, reducing the likelihood of hedge fund activism against these companies in particular.

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TABLE 2 Alternative definitions of family firms.

	Alternative definitions of Family Firm (independent variable)	[1] Coeff. (DV: Activist Targeted)	[2] Coeff. (DV: CAR)
Family directors			
D	**One or more family members are directors** (*Firm-year observations*: *1377 FF*, *3556 NFF*; *Campaigns*: *121 against FF*, *337 against NFF*)	−0.450 (.018)	0.021 (.024)
Family ownership			
B	**One or more family members are blockholders** (*Firm-year observations*: *826 FF*, *4082 NFF*; *Campaigns*: *95 against FF*, *363 against NFF*)	0.249 (.286)	0.004 (.619)
Family management			
O	**One or more family members are officers** (*Firm-year observations*: *796 FF*, *4137 NFF*; *Campaigns*: *90 against FF*, *368 against NFF*)	−0.266 (.217)	0.009 (.381)
CEO	**Family CEO** (*Firm-year observations*: *661 FF*, *4272 NFF*; *Campaigns*: *81 against FF*, *377 against NFF*)	0.130 (.562)	0.006 (.542)
FCEO	**Founder CEO** (*Firm-year observations*: *357 FF*, *4576 NFF*; *Campaigns*: *52 against FF*, *406 against NFF*)	0.104 (.743)	−0.005 (.632)
DCEO	**Descendant CEO** (*Firm-year observations*: *304 FF*, *4629 NFF*; *Campaigns*: *29 against FF*, *429 against NFF*)	0.090 (.806)	0.011 (.308)
Villalonga and Amit (2006) definitions			
1	**One or more family members are officers, directors, or blockholders** (*Firm-year observations*: *1440 FF*, *3493 NFF*; *Campaigns*: *126 against FF*, *332 against NFF*)	−0.527 (.006)	0.020 (.025)
2	**At least one family officer and one family director** (*Firm-year observations*: *790 FF*, *4143 NFF*; *Campaigns*: *90 against FF*, *368 against NFF*)	−0.468 (.014)	0.021 (.024)
3	**Family is largest voteholder** (*Firm-year observations*: *752 FF*, *4042 NFF*; *Campaigns*: *86 against FF*, *343 against NFF*)	−0.014 (.956)	0.001 (.888)
4	**Family is largest shareholder** (*Firm-year observations*: *682 FF*, *4112 NFF*; *Campaigns*: *78 against FF*, *351 against NFF*)	−0.040 (.874)	0.001 (.944)
5	**One or more family members from second or later generation are officers, directors, or blockholders** (*Firm-year observations*: *814 FF*, *4119 NFF*; *Campaigns*: *57 against FF*, *401 against NFF*)	−0.481 (.023)	0.033 (.001)
6	**Family is largest voteholder and has at least one family officer and one family director** (*Firm-year observations*: *492 FF*, *4302 NFF*; *Campaigns*: *66 against FF*, *363 against NFF*)	−0.442 (.020)	0.021 (.026)
7	**Family is largest shareholder and has at least 20% of votes** (*Firm-year observations*: *427 FF*, *4367 NFF*; *Campaigns*: *43 against FF*, *386 against NFF*)	−0.555 (.293)	−0.013 (.298)

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TABLE 2 (Continued)

Alternative definitions of Family Firm (independent variable)		[1] Coeff. (DV: Activist Targeted)	[2] Coeff. (DV: CAR)
8	**One or more family members are directors or blockholders, but there are no family officers** (*Firm-year observations*: *644 FF*, *4289 NFF*; *Campaigns*: *36 against FF*; *422 against NFF*)	−0.484 (.037)	0.017 (.050)
9	**Family is the largest voteholder, has at least 20% of votes, one family officer and one family director, and is in the second or later generation** (*Firm-year observations*: *256 FF*, *4538 NFF*; *Campaigns*: *18 against FF*, *411 against NFF*)	−0.530 (.085)	−0.003 (.852)

The rows in this table present the coefficients and *p*-values (in parentheses) for the Family Firm variable, using different definitions of family firms

These coefficients are each derived from separate regressions whose dependent variables are Activist Targeted in Column [1] and CAR in Column [2]

The analyses are conducted at the firm-year level for the regressions in Column [1] and at the campaign-level for the regressions in Column [2]

These regressions include all the control variables and fixed effects shown in Table 1, with robust standard errors clustered by firm

and control structures, is the key impediment to hedge fund activism, as well as the main driver of the outsize returns to announcements of activist hedge fund campaigns against family firms.

4.2.2 | Campaign tactics and costs

To test our argument that activist hedge funds are more likely to use hostile tactics in their campaigns against family firms than nonfamily firms, we estimate the likelihood of activist hedge funds engaging in demand negotiations, seeking board representation, and launching proxy fights (Gantchev, 2013). Results appear in Table 4. The positive coefficients on *Family Firm* in all three models indicate that activist hedge funds are more likely to use these campaign tactics against family firms than nonfamily firms. Transforming coefficients to odds ratios, relative to nonfamily firms, activist hedge funds are twice as likely to engage in demand negotiations with family firms (Model [1]), nearly four times as likely to seek board representation (Model [2]), and more than three times as likely to initiate proxy fights against family firms (Model [3]). Together, these results support our argument that activist hedge funds are more likely to use hostile campaign tactics against family firms than nonfamily firms.[11]

[11]Selection could be driving these results to the extent that certain activist hedge funds are more likely to initiate campaigns against family firms, and those activist hedge funds happen to favor more hostile tactics. To explore this possibility, we compared the identities of the top 10 activist hedge funds that initiated campaigns against family versus nonfamily firms. Nine out of the top 10 activist hedge funds that initiated campaigns against family and nonfamily firms were identical. This suggests that selection is likely not driving the results in Table 4, since the nearly the exact same activist hedge funds initiate campaigns against family and nonfamily firms.

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TABLE 3 Disaggregating the presence of family members on boards of directors versus in ownership and control structures.

Alternative definitions of Family Firm (independent variable)		[1] Coeff. (DV: Activist Targeted)	[2] Coeff. (DV: CAR)
D	**One or more family members are directors** (*Firm-year observations*: *1377 FF*, *3556 NFF*; *Campaigns*: *121 against FF*, *337 against NFF*)	−0.450 (.018)	0.021 (.024)
D-O1	**One or more family members are directors AND family owns less than 1%** (*Firm-year observations*: *294 FF*, *4614 NFF*; *Campaigns*: *21 against FF*, *437 against NFF*)	−0.600 (.035)	0.033 (.002)
D-O5	**One or more family members are directors AND family owns less than 5%** (*Firm-year observations*: *579 FF*, *4329 NFF*; *Campaigns*: *31 against FF*, *427 against NFF*)	−0.897 (.000)	0.027 (.026)
D-O10	**One or more family members are directors AND family owns less than 10%** (*Firm-year observations*: *751 FF*, *4157 NFF*; *Campaigns*: *51 against FF*, *407 against NFF*)	−0.484 (.026)	0.018 (.036)
D-V20	**One or more family members are directors AND family has less than 20% of votes** (*Firm-year observations*: *857 FF*, *4051 NFF*; *Campaigns*: *67 against FF*, *391 against NFF*)	−0.327 (.074)	0.021 (.012)
D-V33	**One or more family members are directors AND family has less than 33% of votes** (*Firm-year observations*: *999 FF*, *3909 NFF*; *Campaigns*: *78 against FF*, *380 against NFF*)	−0.383 (.036)	0.023 (.009)

The rows in this table present the coefficients and *p*-values (in parentheses) for the Family Firm variable, using different definitions of family firms

These coefficients are each derived from separate regressions whose dependent variables are Activist Targeted in Column [1] and CAR in Column [2]

The analyses are conducted at the firm-year level for the regressions in Column [1] and at the campaign-level for the regressions in Column [2]

These regressions include all the control variables and fixed effects shown in Table 1, with robust standard errors clustered by firm

Taking these ideas a step further, Gantchev (2013) estimates the average dollar costs of activist hedge funds engaging in demand negotiations ($2.94 million), seeking board representation ($1.83 million), and launching proxy fights ($5.94 million). We use these figures to estimate and compare the average cost of activist hedge fund campaigns against family and nonfamily firms. We find that the average cost of an activist hedge fund campaign against a family firm is $3.70 million, while it is $3.18 million for nonfamily firms ($p = .019$).[12]

[12]The difference in the average duration of activist hedge fund campaigns against family firms versus nonfamily firms is less pronounced: 124 days versus 112 days ($p = .3976$).

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TABLE 4 Campaign tactics.

Dependent variables	[1] Demand negotiation	[2] Board seats sought	[3] Proxy fight
Family firm	0.798 (.050)	1.350 (.003)	1.146 (.007)
ln(total sales)	0.295 (.054)	−0.113 (.686)	−0.124 (.607)
Tobin's *q*	−0.010 (.956)	−0.148 (.453)	−0.231 (.233)
Return on assets	−1.869 (.211)	−0.871 (.295)	−0.627 (.404)
Capital intensity	−2.292 (.133)	−3.687 (.129)	−2.246 (.297)
Leverage	−0.249 (.742)	1.899 (.161)	1.453 (.257)
Interest coverage ratio	0.001 (.029)	−0.009 (.385)	−0.009 (.334)
Cash ratio	0.348 (.767)	1.832 (.222)	0.816 (.611)
Firm age	0.004 (.588)	−0.004 (.720)	−0.007 (.423)
Unrelated diversification	−1.614 (.036)	−1.007 (.505)	−0.865 (.507)
Acquisition intensity	−0.051 (.217)	−0.198 (.025)	−0.217 (.007)
Firm growth	−0.226 (.641)	−1.214 (.220)	−0.876 (.314)
CEO turnover	0.280 (.416)	−0.085 (.834)	0.064 (.868)
CEO duality	−0.188 (.560)	0.020 (.959)	0.309 (.412)
CEO age	0.018 (.388)	0.028 (.383)	0.001 (.975)
CEO incentive compensation	−0.316 (.590)	−1.784 (.109)	−1.950 (.048)
CEO stockholding	−0.063 (.063)	−0.001 (.989)	−0.033 (.486)
Board size	0.078 (.263)	0.285 (.003)	0.270 (.002)
Board ownership	0.421 (.854)	−4.727 (.127)	−3.567 (.073)
Average board tenure	−0.021 (.707)	−0.195 (.005)	−0.164 (.010)
Average board experience	−0.005 (.903)	−0.012 (.907)	0.003 (.969)
Total institutional ownership	0.452 (.463)	1.113 (.187)	1.069 (.192)
Dual class share	0.606 (.487)	−10.861 (.000)	−11.618 (.000)
Ownership-vote wedge	−1.058 (.336)	12.533 (.000)	13.402 (.000)
G-index	−0.010 (.910)	−0.104 (.348)	−0.095 (.341)
Firm transparency	0.562 (.536)	2.750 (.016)	2.609 (.008)
Analyst coverage	0.009 (.709)	−0.017 (.504)	−0.001 (.959)
Analyst forecast accuracy	1.781 (.041)	−10.634 (.113)	−10.647 (.121)
Industry concentration	−0.820 (.811)	−0.744 (.588)	−0.885 (.503)
Industry sales growth	0.019 (.087)	0.004 (.689)	−0.010 (.462)
Constant	−3.131 (.154)	−4.117 (.199)	−2.518 (.360)
Year fixed effects	Yes	Yes	Yes
Industry fixed effects	Yes	Yes	Yes
Level of analysis	Campaign-level	Campaign-level	Campaign-level
Specification	Logistic	Logistic	Logistic
Pseudo-R^2	.100	.231	.209
Number of observations	559	559	559

Robust standard errors are clustered by firm

p-Values are in parentheses

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One potential counterpoint to our argument about the link between the higher cost of hedge fund activism in family firms and higher expected returns to these campaigns is that hedge fund activism may be less likely to succeed against family firms than nonfamily firms. If this is indeed the case, the greater number of unsuccessful campaigns against family firms would be expected to attenuate the favorable returns to hedge fund activism in family firms. This could reduce or even eliminate our prediction in Hypothesis 2 regarding the difference in the returns to announcements of activist hedge fund campaigns against family firms versus nonfamily firms. We explore this possibility by testing whether activist hedge fund campaigns against family firms are indeed less successful than those against nonfamily firms. We find evidence to the contrary (results appear in Appendix Table A4): activist hedge funds are about 12 times more likely to win proxy fights against family firms than nonfamily firms ($p = .041$) and about eight times more likely to attain board representation in family firms than nonfamily firms ($p = .000$).

While these results bolster our prediction and finding of higher returns to announcements of activist hedge fund campaigns against family firms than nonfamily firms, we also test whether the *cost-adjusted* announcement returns to activist hedge fund campaigns against family firms exceed those of nonfamily firms (Gantchev, 2013). We find a 1.4% difference in the cost-adjusted announcement returns to activist hedge fund campaigns against family versus nonfamily firms ($p = .021$). Even when we account for the greater cost of hedge fund activism against family firms, these campaigns still outperform those that are initiated against nonfamily firms.

4.2.3 | Campaign demands

We argued that the higher expected returns to activist hedge fund campaigns against family firms may be driven by the fact that the problems in these companies are worse than those in nonfamily firms, thus making it worthwhile for activist hedge funds to incur the relatively higher costs of initiating campaigns against family firms. To explore whether this is the case, we estimate the likelihood of activist hedge funds making the following demands in their campaigns: (a) scope changes, including divestitures, corporate breakups, or strategic reviews; (b) board changes, specifically, seeking board representation; (c) governance changes, including the removal of takeover defenses and other governance demands; (d) management changes, including the removal of certain officers and compensation changes; and finally, (e) financial changes (e.g., capital structure enhancements, returning cash to shareholders).

Results appear in Table 5. Activist hedge funds are more likely to demand that family firms divest certain businesses, sell or break up their entire companies (Chen & Feldman, 2018), and remove their takeover defenses, all relative to nonfamily firms. Consistent with our earlier results, activist hedge funds are also more likely to seek board seats in their campaigns against family firms than nonfamily firms. However, there are no differences between family and nonfamily firms in the likelihood of activist hedge funds demanding strategic reviews, other governance changes, or any of the management or financial changes listed in Table 5. Together, these results suggest that the changes activist hedge funds demand in family firms are more substantive than in nonfamily firms, cutting to the heart of the governance and performance shortcomings that often plague family firms. In contrast, it is telling that activist hedge funds are equally likely to demand the less substantive changes in family and nonfamily firms.

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4.3 | Robustness tests

4.3.1 | Definition of nonfamily firms

We conduct a series of analyses to test the robustness of our results to various considerations. The first of these is the definition of nonfamily firms. Thus far, our analyses have implicitly categorized all firms that are not family firms (variously defined) as nonfamily firms. However, this simple classification may mask the heterogeneity among firms we do not classify as family firms, especially regarding their ownership structures. As such, we vary the definition of nonfamily firms to see whether these changes influence our results.

In Appendix Table A5, we present the key coefficients from regressions predicting the likelihood of and returns to activist hedge fund campaigns. In this table, family firms are defined as those in which one or more family members are officers, directors, or blockholders. In Models [1] and [2], nonfamily firms are defined as those in which no family members are officers, directors, or blockholders, *and* blockholders do not own more than 20% of the firm's outstanding shares. This representation of nonfamily firms therefore requires that nonfamily firms have widely dispersed ownership structures. In Models [3] and [4], nonfamily firms are defined as those in which no family members are officers, directors, or blockholders, *and* the firm has no dedicated institutional investors (Bushee, 1998). Dedicated institutional investors own large, long-term stakes in a small number of firms. Accordingly, excluding dedicated institutional investors from the definition of nonfamily firm effectively requires that these companies only have shorter-term institutional investors. Finally, Models [5] and [6] revert to the original definition of nonfamily firms (those in which no family members are officers, directors, or blockholders) but incorporate additional controls for the percentage of ownership held by dedicated and transient institutional investors. This provides an alternate way of testing how the composition of ownership influences the likelihood of and returns to hedge fund activism in family versus nonfamily firms.

Appendix Table A5 reveals that regardless of the definition of nonfamily firms, activist hedge funds are less likely to initiate campaigns against family firms than nonfamily firms (Models [1], [3], and [5]), and the returns to announcements of activist hedge fund campaigns against family firms exceed those of nonfamily firms (Models [2], [4], and [6]).[13] Thus, varying the definition of nonfamily firms does not appear to influence our results.

4.3.2 | Propensity score matching

A potential empirical challenge in this article arises from the possibility that there may be fundamental differences in the characteristics of family and nonfamily firms, which could explain any observed differences in the likelihood of and returns to activist hedge fund campaigns against these companies. We use PSM to mitigate the confounding effects of these observable

[13]In Model [6], the coefficient on *% Owned by Dedicated Institutional Investors* is positive ($p = .064$), indicating that the percentage ownership held by dedicated institutional investors is positively associated with the cumulative abnormal returns to activist hedge fund campaigns. This makes intuitive sense: given their long-term holdings, dedicated institutional investors would be expected to benefit disproportionately from the changes that activist hedge funds demand in their campaigns.

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TABLE 5 Campaign demands.

Campaign demands (Dependent variables)	Coeff. on Family Firm (Independent variable)
Scope changes	
Break up company/divest (activist is pressuring the company to divest certain businesses or divisions through a sale, spin-off, or split-up, or focus its resources on its "core business")	2.305 (.000)
Seek sale/merger/liquidation (activist is agitating for a sale or liquidation of the entire company)	2.622 (.001)
Review strategic alternatives (activist is urging the board to review strategic alternatives)	1.543 (.107)
Board changes	
Board seats (activist is seeking board seats through either a proxy fight or a non-proxy fight)	1.817 (.000)
Governance changes	
Remove takeover defenses (activist is pressuring the company to remove takeover defenses)	1.732 (.043)
Other governance enhancements (other governance enhancements that do not fall into the "remove takeover defenses" objective category)	1.809 (.188)
Management changes	
Remove officers (activist group is seeking to remove or replace a member of the upper management)	1.059 (.352)
Compensation-related enhancements (activism related to executive pay including all golden parachutes and excessive severance agreements/takeover defenses)	0.004 (.996)
Financial changes	
Capital structure (activist is pressuring the company to change its capital structure, either by increasing or decreasing leverage)	1.215 (.194)
Return cash via dividends/buybacks (activist is pressuring the company to return cash to shareholders through share repurchases, increases in regular quarterly dividends, or the issuance of one-time special dividends)	−0.221 (.750)

The rows in this table present the coefficients and *p*-values (in parentheses) for the Family Firm variable

These coefficients are each derived from separate regressions whose dependent variables are the various campaign demands

The analyses are conducted at the campaign-level for all regressions

These regressions include all the control variables and fixed effects shown in Table 1, with robust standard errors clustered by firm

differences between family and nonfamily firms before estimating both the relative likelihood of and returns to activist hedge fund campaigns.

The first stage of our PSM model matches family and nonfamily firms on their observable characteristics. We use a logistic regression to estimate a firm's propensity to be a family firm,

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meaning that the dependent variable is *Family Firm*. The independent variables represent the observable characteristics that distinguish family firms and nonfamily firms. We use the predicted values from this first-stage regression to generate propensity scores for all family (treatment group) and nonfamily firm (control group) observations. By eliminating observations off the common support of the resulting joint distribution of propensity scores, we ensure that any combination of characteristics observed in the treatment group is also observed among the control group, and vice versa. Our base match specification uses nearest neighbor matching with a caliper of 0.01 to generate a one-to-three matched sample of treatment and control group observations.[14]

Results from the first stage of the PSM model appear in Appendix Table A6, and balance tests comparing the characteristics of the unmatched and matched treatment and control groups appear in Appendix Table A7. In the unmatched sample, family and nonfamily firms exhibit sizeable differences in 14 of the 18 covariates included in the first-stage regression of the PSM model. In the matched sample, however, these differences are substantially reduced, suggesting that the treatment and control groups in the matched sample are observationally similar to one another. This suggests that the PSM model attenuates the bias that may have resulted from preexisting differences between family and nonfamily firms.

In the second stage of the PSM model, using only the matched sample of family and nonfamily firms, we predict the relative likelihood of activist hedge funds initiating campaigns against these two types of firms, as well as investors' reactions to announcements of these campaigns. Results of these second-stage regressions appear in Appendix Table A8. Activist hedge funds remain less likely to initiate campaigns against family firms than nonfamily firms (Model [1]), and the returns to announcements of activist hedge fund campaigns against family firms continue to exceed those of nonfamily firms (Model [2]). These findings provide evidence that our results are not sensitive to the use of matching to attenuate the effects of observable differences between family and nonfamily firms (DesJardine & Durand, 2020).

5 | DISCUSSION

5.1 | Contributions

Activist hedge funds have traditionally been conceptualized as targeting firms that have problems and seeking to redress those issues (Boyson & Mooradian, 2011; Clifford, 2008; Denes et al., 2017; DesJardine et al., 2021; DesJardine & Shi, 2023; Klein & Zur, 2009). However, recent research on hedge fund activism has begun to consider how *opportunities* might equally influence which firms activist hedge funds target. Our study adds to this important work in two main ways.

First, DesJardine, Shi, and Marti (2023) argue and find evidence that activist hedge funds are more likely to initiate campaigns against firms that have problems when there are also greater opportunities to exert influence. However, campaigns against firms that have problems but are *worse* opportunities for hedge fund activism of course do occur. This raises an interesting question: what makes it worthwhile for activist hedge funds to initiate campaigns against these companies? Our study answers this question: when opportunities to exert influence in

[14]We test the robustness of this model using one-to-one, one-to-three, and one-to-five matched samples with caliper sizes of 0.01, 0.05, and 0.1, and results are consistent with our main findings.

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particular firms (e.g., family firms) are worse, it may only be worthwhile for activist hedge funds to justify the high costs of initiating campaigns against them if their problems are sufficiently severe as to generate greater expected returns. This reinforces the insight that the traditional view of hedge fund activism as seeking to redress problems may be incomplete, and that the interaction between opportunities and problems determines the propensity of hedge fund activists to target certain firms. Whereas DesJardine, Shi, and Marti (2023) establish that problems require better opportunities to make activist hedge funds initiate campaigns against certain firms, our study shows that worse opportunities require bigger problems to make it worthwhile for activist hedge funds to initiate campaigns. In other words, when the likelihood of a potential payout from hedge fund activism is high, the expected size of that payout can be smaller, but when the likelihood of a potential payout from hedge fund activism is lower, the expected size of that payout must be correspondingly larger.[15]

Second, DesJardine, Shi, and Marti's (2023) empirical representation of companies that present better opportunities for hedge fund activism is the demographic diversity of their boards, which may make firms slower and less united in their responses to hedge fund activism. Accordingly, one of the main contributions of DesJardine, Shi, and Marti (2023) is to document the critical importance of boards of directors as a determinant of the incidence (or lack thereof) of hedge fund activism. Our study offers further support for this insight by showing that in family firms, the presence of family members on family firms' boards of directors makes these companies worse opportunities for hedge fund activism (e.g., Kastiel, 2016). Our findings therefore reinforce the idea that various characteristics of firms' boards of directors may indeed shape corporate opportunity structures, and hence, activist hedge funds' expectations of the likelihood of success or failure in their campaigns, thereby making certain companies more (or less) attractive candidates for hedge fund activism than others.

Further to this point, the literature on family firms has explored how founding families may insulate themselves from outside influence, especially through the composition of their boards of directors (Anderson & Reeb, 2004) and the use of control-enhancing mechanisms such as dual-class shares, pyramids, crossholdings, or voting agreements (La Porta et al., 1999; Villalonga et al., 2015; Villalonga & Amit, 2006, 2009, 2010, 2020). Research has even considered how some of these very same mechanisms might insulate family (or "controlled") firms from hedge fund activism specifically (Kastiel, 2016). Our study contributes to this body of work by delving deeper into the critical role that family directors may play in the governance of these organizations.

While existing studies have documented the importance of the board of directors as a governance mechanism that might impede hedge fund activism in companies generally (DesJardine, Shi, & Marti, 2023), these effects are likely to be pronounced in family firms. Specifically, family directors have a disproportionate voice on their firms' boards, due both to the strength of their financial incentives and to the deference that other board members may exhibit to their wishes (Lansberg, 2022). Accordingly, family directors may serve as an implicit deterrent (Baumol et al., 1986) to hedge fund activism: recognizing that family directors are likely to be involved in crafting their firms' responses to hedge fund activism and that other directors are likely to support them, activist hedge funds may be disinclined to initiate campaigns against family firms, especially those in which family members serve on the board (Kastiel, 2016). This insight is the linchpin for this article's findings, since it explains both why activist hedge funds may be less

[15]Thus, for activist hedge funds, targeting both family and nonfamily firms may be a diversification strategy of sorts: nonfamily firm campaigns are lower risk, lower return, while family firm campaigns are higher risk, higher return.

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likely to initiate campaigns against family firms and why it may be more costly for them to do so, which in turn drives the outsize returns to activist hedge fund campaigns against family firms.

Finally, research has extensively considered the relative costs and effectiveness of various governance mechanisms. Although internal governance mechanisms like independent directors, managerial incentives, and passive institutional investors are relatively cheap (and common) to have in place in almost every firm, they are also not completely effective at preventing value-destroying behavior (e.g., Appel et al., 2016; Feldman & Montgomery, 2015; Hambrick & Jackson, 2000). However, while external governance mechanisms—specifically, the market for corporate control—are usually more effective at limiting such behavior, it is expensive for hostile bidders to mount and execute disciplinary takeovers of undervalued companies (e.g., Walsh & Seward, 1990). In some sense, then, in most firms, hedge fund activism occupies the middle ground between these two poles. Unlike hostile takeovers, activist hedge funds can drive strategic change in firms without having to acquire controlling stakes in them, making hedge fund activism more cost-effective than the market for corporate control. Similarly, while the magnitude of strategic change induced by activist hedge funds is usually greater than what internal governance mechanisms can achieve, it likely falls short of what might occur in a full-scale takeover.

Our paper shows that among family firms specifically, this picture changes. The high cost of hedge fund activism (Gantchev, 2013) pushes its cost closer to that of the market for corporate control in family firms. Equally, though, the tactics used and demands made in activist hedge fund campaigns against family firms could also shift its effectiveness at driving major strategic change closer to that of the market for corporate control. As discussed previously, the problems in family firms may be worse than those in nonfamily firms (e.g., Calabrò et al., 2018; Feldman et al., 2016; Gómez-Mejía et al., 2010; Villalonga & Amit, 2008). This suggests that while activist hedge funds may be able to resolve problems in firms generally, they may be able to do so to a greater extent in family firms specifically. This underscores the point that family firms often exhibit the worst inefficiencies, making hedge fund activism against them especially valuable.

5.2 | Open questions and directions for future research

Our study leaves some questions unanswered, opening promising directions for future research. One involves the tension that seems to emanate from our two main findings: although activist hedge funds are less likely to initiate campaigns against family firms, on average, they enjoy a 200-basis point gain from doing so (relative to initiating campaigns against nonfamily firms). Since activist hedge funds are motivated by the initial bump in their targets' share prices (DesJardine & Durand, 2020), why, then, wouldn't they be *more* rather than *less* likely to initiate campaigns against family firms? Furthermore, since other investors seem to support activist hedge funds' interventions in family firms (as evidenced by the greater CAR that accompany announcements of these campaigns), couldn't activist hedge funds get away with using *less* rather than *more* hostile tactics against these firms?

A potential answer to both questions is that other investors may be more optimistic about activist hedge funds' prospects of driving change in family firms than the activist hedge funds are themselves. This explanation makes sense from the perspective of both activist hedge funds and investors in the firms they target. Activist hedge funds may recognize ex ante the fact that family firms' board, ownership, and control structures will make it difficult for them to

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gain and exert influence in these companies (Kastiel, 2016), suggesting a need to use more hostile tactics to ensure success in initiating campaigns against them. Investors may interpret the high costs of utilizing hostile tactics against family firms as a sign that share price improvements will follow the initiation of campaigns against these companies (Appel et al., 2019; Gantchev, 2013). Together, these points suggest that investors may indeed expect a greater upside from campaigns against family firms than nonfamily firms than activist hedge funds do themselves. Future research could explore this tension and its ramifications by shedding light on the perceptions and motivations of the parties involved in hedge fund activism in family and nonfamily firms.

Another question that arises from our study is whether there are differences in the implications of hedge fund activism against family versus nonfamily firms for stakeholders other than investors. A growing body of literature has begun to examine the implications of hedge fund activism for actors other than shareholders and for measures other than investor returns (Chen et al., 2021; DesJardine & Durand, 2020; Shi et al., 2021). Importantly, though, family firms are known to interact with their stakeholders in different ways than nonfamily firms (e.g., Berrone et al., 2010). This suggests that it would be interesting to explore the implications of hedge fund activism in family versus nonfamily firms for stakeholder-oriented measures of performance. Relatedly, we have limited the scope of our analysis to activist hedge fund campaigns in which demands were *not* social, environmental, or political in nature. However, hedge fund activism in pursuit of such objectives is growing in importance (e.g., Carl Icahn's campaigns against McDonald's and Kroger). Thus, it would be interesting to examine the implications of hedge fund activism geared at achieving such demands in family and nonfamily firms.

6 | CONCLUSION

In summary, hedge fund activism is a multifaceted phenomenon that has come to be of significant interest to scholars of strategic management. It interacts with numerous aspects of firms' strategies, including their corporate scope decisions, operational processes, governance practices, and even their approaches to stakeholder management. This study has extended this body of research by examining the interplay between hedge fund activism and family firms, introducing a new dimension to the rich and ongoing conversation about this topic.

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DATA AVAILABILITY STATEMENT

Research data are not shared.

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