Institutional Investor

Blue Harbour Takes 'Friendly' Stake in AGCO

Clifton Robbins's firm holds talks with a farm equipment supplier that appears ripe for improvement. BY Stephen Taub

Shares of AGCO Corp. surged about 2.5 percent Friday after Clifton Robbins's Blue Harbour Group disclosed the night before that it had taken an activist position in the farm equipment manufacturer.

The Greenwich, Connecticut, hedge fund firm said in a regulatory filing that it boosted its stake to nearly 4.7 million shares, or 5.3 percent of the total outstanding. At the end of the first quarter, AGCO was Blue Harbour's seventh-largest holding.

In the filing, the hedge fund firm says the stock "represented an attractive investment opportunity."

The filing also said that Robbins and others at his firm have already had discussions with management and directors as well as other interested parties such as analysts, other shareholders, financial professionals and others "regarding a variety of matters," including the company's business, management, capital structure and allocation, corporate governance, board composition, and strategic alternatives and direction.

Blue Harbour also warned that it "may take other steps seeking to bring about changes to increase shareholder value."

Robbins, who likes to call himself a "friendly activist" because he prefers to work closely with management, declined to comment.

AGCO, which has a $4.7 billion market capitalization, is the world's third-largest maker of farm equipment. The company generates 75 percent of its business from outside the U.S., half in Europe.

The company has essentially been a roll-up of other smaller companies since about 2004.

Revenue fell more than 9 percent in 2014, while earnings plummeted 31 percent.

At least one individual familiar with the company says the 2012 drought that drove up corn and soybeans prices gave a temporary boost to firms like AGCO for a couple of years as rising prices of commodities led to big demand for AGCO's products, especially in the U.S. and Brazil.

S&P Capital IQ said in a recent report that it is looking for another 20 percent decline in revenues this year, followed by a flat 2016. "Demand for AGCO's products are likely to be impacted by reductions in farm income, which hit a peak in 2013, and is likely to decline over the next two years," the financial data and analytics firm added, keeping its Hold rating on the stock. This will place pressure on operating margins, it said.

AGCO's overseas earnings have also been hurt by currency hedging.

However, Barclays, which has a more bullish outlook and an Equal Weight rating, pointed out that Europe is "showing very early signs of stabilizing at low levels." This could "provide a lift" to the stock, it added.

"Arguably more importantly though is that management's relatively aggressive restructuring actions and intense focus on cost control seems to be bearing fruit," Barclays said.

Interestingly, on June 17 — just one day before Blue Harbour filed its 13D — Morgan Stanley machinery analyst Nicole DeBlase published a 72-page report analyzing how various companies in the sector could improve their operations.

The most intriguing part of the report: DeBlase ran screens "based on themes of recent activist campaigns" to determine which companies could hypothetically pursue what she called "self-help strategies to improve their results."

She singled out four criteria for candidates: share price underperformance, margin underperformance compared to their peers, underutilized balance sheets and portfolio change.

She then identified two companies she deemed could most benefit from a focus on each of these themes "with clear opportunity for structural change."

The two companies are AGCO and Terex Corp.

AGCO is among four companies Morgan Stanley singles out for potential margin improvement.

It is also one of three companies singled out for balance sheet "optionality," noting that they "appear most underlevered."

Even so, DeBlase warned that "activism has not been a panacea in the industrials space."

She noted that shareholder activist campaigns tend to target underperformers. "But subsequent share price performance has been mixed," the report noted.

We'll see how Blue Harbour fares.