

STRATEGIC ACTIVISM AND NONMARKET STRATEGY

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Activist NGOs have increasingly foregone public politics and turned to private politics to change the practices of firms and industries. This paper focuses on private politics, activist strategies, and nonmarket strategies of targets. A formal theory of an encounter between an activist organization and a target is presented to examine strategies for lessening the chance of being a target and for addressing an activist challenge once it has occurred. The encounter between the activist and the target is viewed as competition. At the heart of that competition is an activist campaign, which is represented by a demand, a promised reward if the target meets the demand, and a threat of harm if the target rejects the demand. The model incorporates target selection by the activist, proactive measures and reputation building by a potential target to reduce the likelihood of being selected as a target, fighting a campaign, and credible commitment.

1. INTRODUCTION

Political and social activists are increasingly important components of the environment of business. The goal of activism typically is to influence firm and industry practices, often motivated by social or ethical concerns. To change the practices of potential target firms, activists engage in private and public politics. Public politics strategies

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focus on advancing the activist's agenda through public institutions such as legislatures, executive agencies, and courts. Many activists have concluded that public politics is too easily blocked and have turned to private politics instead. Private politics refers to actions by private interests such as activists that target private agents, often in the institution of public sentiment.¹ Michael Brune, executive director of the Rainforest Action Network (RAN) commented that "Companies were more responsive to public opinion than certain legislatures were. We felt we could create more democracy in the marketplace than in the government."² Democracy in the marketplace means that citizen consumers express in markets their assessment of firm and industry practices. If they object to logging in old growth forests, they can impose their will on timber companies by refusing to buy old growth products. Commenting on the boycott campaign against Exxon Mobil for its stance on climate change, Paul Gilding, former head of Greenpeace, said, "The smart activists are now saying, 'OK, you want to play markets—let's play.' [Lobbying government] takes forever and can easily be counter-lobbied by corporations. No, no, no. They start with consumers at the pump, get them to pressure the gas stations, get the station owners to pressure the companies and the companies to pressure governments. After all, consumers do have choices where they buy their gas, and there are differences now. Shell and BPAmoco (which is also the world's biggest solar company) both withdrew from the oil industry lobby that has been dismissing climate change."³ After the Senate failed to increase fuel economy standards, executive director Carl Pope of the Sierra Club announced, "we're going now to the customers."⁴ This paper focuses on activists that campaign against their targets and not on NGOs that cooperate with firms. The former create demand for the latter.

Although many activist organizations such as the Sierra Club engage in both private and public politics, this paper focuses on private politics, activist strategies, and nonmarket strategies of targets. The paper presents foundations of nonmarket strategy developed from a formal theory that focuses on an encounter between an activist organization and a target. The objective is to examine strategies for lessening the chance of being a target and for addressing an activist challenge once it has occurred.⁵ To develop nonmarket strategy foundations for private politics, the encounter is viewed as strategic competition. At the heart of

1. Baron (2003a) introduces the concept of private politics.

2. Baron and Erin (2004a).

3. *The New York Times*, June 2, 2001.

4. *The Wall Street Journal*, August 20, 2002.

5. Bonardi (2005) considers target strategies for dealing with "destructive activists" with a focus on possible adverse effects of the strategies. The strategies considered are prosecution, public denial, and collaboration, and the possible adverse effects are media attention and solidarity among activists.

that competition is an activist campaign. A campaign consists of an issue such as environmental protection, a target, which could be a firm or an industry, and a strategy for success. A campaign can have effects at two levels. At one level a campaign can affect the practices of the target to which the activist objects. Such threats require a responsive strategy as well as a proactive strategy by potential targets to reduce the likelihood of being targeted. At the other level a campaign can affect supply in an industry. A successful activist campaign can reduce the returns in an industry by increasing costs and reducing demand. Activist campaigns opposing the use of old growth timber and supporting stringent forest stewardship programs increase the cost of timber and products made with wood. These effects can reduce investment in the industry.

Even if the goal is to affect an entire industry, an activist campaign may be targeted at a specific firm for strategic reasons. First, by targeting one firm rather than many, activists lower the participation costs for citizen consumers. For example, the cost to motorists of not buying gasoline from one particular oil company is low but the cost is very high not to buy gasoline at all. Second, a successful campaign against one firm may lead to a domino effect as competing firms attempt to avoid being targeted next by proactively anticipating the activist's demands. Activists may also ratchet up their demands, demanding greater concessions from their second target than their first. Industry-wide changes resulting from an activist campaign may be characterized as private regulation, which can be viewed as an alternative to or substitute for government regulation. Proactive measures by potential targets represent self-regulation, albeit self-regulation induced by the threat of strategic activism.⁶ The self-regulation and private regulation resulting from activist pressure are sometimes labeled as corporate social performance.

A campaign also can affect the supply of activism. The public as consumers may join in a campaign to harm or reward the target. To succeed, campaigns must draw support from the public whether as participants, donors, or volunteers. To influence industry practice, citizens direct their contributions to effective activist groups. This creates competition among activist groups in the market for donors and volunteers. A campaign may be viewed as a local public good for those citizens sympathetic to the activist's cause. The support provided by sympathetic citizens depends on both the accomplishments of the activists, the willingness of individuals to contribute, and the severity of the free-rider problem. Public support and the supply of activism thus is endogenous to campaign strategies.

6. Self-regulation may also be present in public regulation, as firms attempt to avoid additional regulation, as in Maxwell et al. (2000). Self-regulation has also been promoted by regulators through voluntary programs (Segerson and Miceli, 1998).

Operating in an activist-rich environment requires three types of strategies for potential targets. One is a proactive strategy to reduce the likelihood or severity of a campaign. Such strategies could involve reputation building or proactive changes in practices. Second, an actual target needs a strategy for dealing with the campaign. The third type of nonmarket strategy is directed at the supply of activism, which depends on both the public support for the activists' agenda and the costs of conducting a campaign. Strategies focus on reducing the support from the public, raising the cost of activism, and restraining activists' actions.

2. THE PARADIGM: THE CAMPAIGN

2.1 TYPES OF CAMPAIGNS

The paradigm for activist-driven private politics is the campaign. Activists conduct two types of campaigns. In direct or corporate campaigns activists target the firm whose practices they want changed. In indirect or market campaigns activists target an element of the firm's value chain such as a customer or supplier. The cost of directly harming an industrial products firm may be very high, because it is difficult to enlist the participation of the public. But even an industrial products firm can be vulnerable through its value chain. In its campaign to stop logging in old growth forests, RAN did not initially target timber companies, such as Boise Cascade, but instead targeted their customers.⁷ Those companies had brands and a public face that the timber companies did not have. RAN targeted Kinko's, which concluded that RAN's demands were consistent with its own environmental policies and quickly pledged to stop purchasing products made from old growth timber. RAN also targeted home improvement companies, beginning with Home Depot because it was the largest and fastest growing company in the industry. Once Home Depot had agreed to phase out its use of old growth lumber, RAN turned its attention to Lowe's. RAN believed that women were more sympathetic to its cause than men, and it had data indicating that women make most home remodeling decisions. (RAN also knew that Lowe's caters to women, whereas Home Depot does not.) Compared to Home Depot, Lowe's has wider aisles and brighter lighting. RAN tailored campaign materials and its advertisements criticizing the company for Lowe's clientele. Lowe's agreed to RAN's demands before any of the advertisements had been run or any campaign materials distributed.

With Kinko's, Home Depot, and Lowe's committed to stop selling old growth products, Boise Cascade faced the loss of a share of its

7. Information about RAN and its strategy was obtained through interviews and from public sources. See Baron and Erin (2004a,b) and *Fortune*, May 31, 2004.

market for old growth timber. Boise Cascade agreed to stop logging in old growth forests, and RAN turned its attention to the rest of the timber industry with Weyerhaeuser as its next target. Consistent with its previous strategy, RAN targeted Trader Joe's, which eventually agreed to stop purchasing paper products from Weyerhaeuser.

Market campaigns can operate "upstream" as well as "downstream" from the ultimate target. While campaigns targeting brand name customers, such as Home Depot and Lowe's, are more familiar, activists also conduct upstream campaigns. In its global finance campaign, RAN targeted the banks that finance environmentally damaging projects in the developing world. An extreme example is the radical animal rights group (Stop Huntingdon Animal Cruelty SHAC) that in its campaign against the animal testing company Huntingdon Life Sciences not only targeted Huntingdon's bank, insurance broker, and auditor but even local taxi companies (Diermeier, 2003).

The threat and actuality of harm to the target are at the center of a campaign. Harm could result from a boycott organized by the activist.⁸ RAN, however, does not use the term boycott, because it has concluded that it is too difficult to demonstrate to targets that sales have been hurt by a campaign. Instead, RAN attempts to harm the target's reputation. In its campaigns RAN organizes Days of Action in which up to 100 demonstrations against a target take place across the United States and in other countries. The harm could also be less direct by generating regulatory risk by attracting politicians and public politics or creating uncertainty that could raise the cost of raising capital.

2.2 A MODEL OF CAMPAIGNS

This section presents a basic model of a campaign to explain the locus of activism and its effect on a target. Consider an activist that seeks to change the practices of a target firm. These could be workplace practices in overseas factories, emissions of pollutants, or aggressive marketing practices as in the case of subprime lending. Suppose the activist makes a demand and can both reward and harm the target. The demand, for example, could be to meet higher workplace standards. The reward could be public praise from the activist if the target changes its practices, inclusion of the target in a list of those who have changed their practices, the grant of a seal, or a credible promise of no subsequent targeting.⁹ Harm can take a variety of forms. It could be a boycott, public criticism, disruption of operations, the staging of events such as demonstrations to attract the media, mobilizing students to impede the target's hiring

8. See Friedman (1999) for studies of boycotts. Baron (2003b), Diermeier (2003), and Innes (2004) provide theories of boycotts.

9. See Feddersen and Gilligan (2001).

or to influence investment or licensing decisions by university officials, damage to the target's reputation, criticizing individual executives, and violence. Delivering harm may provide additional benefits to the activist by attracting the news media, which can be beneficial in raising funds or attracting volunteers for future campaigns. Let the demand be denoted by x_D , the reward by r , and the harm by h . A campaign strategy consists of a triple (x_D, r, h) , which may be interpreted as a take-it-or-leave-it offer of the form, "If you meet our demand x_D , you will receive a reward r . If you do not, you will incur harm h ."¹⁰

Although the model represents a single period, the activist is assumed to have reputational concerns that cause it to follow through with the harm if the target rejects its demand and the reward if the target concedes. The activist may be able to develop a reputation for following through on the harm component of its campaign by harming any target that does not concede to its demand. The activist could develop this reputation through campaigns against many targets, so repetition with the same target is not required.¹¹ The activist must also be able to commit to forego the campaign and deliver the rewards if the target accepts the demand.

In the model the activist moves first by choosing a campaign (x_D, r, h) .¹² The target then either accepts the demand x_D , receiving the reward r , or rejects it, maintaining its current practices and incurring the harm h . In Section 3, a prior stage is introduced in which the target can make *ex ante* concessions or develop a reputation that influences the activist's campaign strategy.

Let the profits of the target be $\pi(x_0)$ if the current practices x_0 are continued and $\pi(x_D)$ if the activist's demand is accepted, where $\pi(x_0) > \pi(x_D)$, $\pi'(\cdot) < 0$, and $\pi(\cdot)$ is concave. For example, x_0 could be paying the market wage, whereas the demand x_D could be paying a living wage. The cost $\pi(x_D) - \pi(x_0)$ to the target of conceding to the activist's demand includes any strategic effects resulting from the target's competitors. Although the activist and the target could bargain over resolving the issue, to simplify the model the demand is assumed either to be accepted or rejected. The target will concede if only if

$$\pi(x_D) + r \geq \pi(x_0) - h. \quad (1)$$

10. The use of harm and rewards in private politics is analogous to the use of taxes and subsidies in public politics and government regulation (Lewis, 1996); Segerson and Miceli, 1998).

11. Activist reputation is considered in Section 5.2 in the context of a repeated moral hazard problem.

12. As discussed above, the activist also chooses a cause and a target. These issues will be considered in Section 2.4.

In contrast to contracting between parties with property rights, an activist campaign makes the target worse off. An activist campaign thus is similar to extortion.¹³

To simplify the exposition, assume that the target can be one of two types. One type is recalcitrant and will not change its practices when targeted in a campaign. The other type is strategic and hence responsive to the campaign and will accept the demand if (1) is satisfied. Let the probability that the target is responsive be p , $p \in [0, 1)$, and $1 - p$ that it is recalcitrant. For example, with probability $1 - p$ the target, on principle, refuses to concede to the coercion of the campaign.¹⁴ The responsive target concedes if the campaign satisfies (1) and otherwise continues its current practice. McDonald's, for example, has been responsive to demands for the humane treatment of food animals. In this section, p is taken as exogenous, and in Section 3.2 it is made endogenous. The probability p can also be interpreted as the probability that the campaign succeeds when the target fights back, as considered in Section 4.

Let the utility of the activist if the target concedes to the demand be $v(x_D)$ and $v(x_0)$ if it does not, where $v(\cdot)$ is strictly increasing. The activist's preferences may be given a number of interpretations. Its preferences could reflect moral concerns such as a gain from a desirable redistribution or mitigation of a negative externality. A cynical interpretation is that the difference $v(x_D) - v(x_0)$ is the funds raised or the career enhancement for the activist as a result of the campaign. The expected utility $U(x_D, r, h)$ from a campaign is

$$U(x_D, r, h) = p(v(x_D) - c(r)) + (1 - p)(v(x_0) - g(h)), \quad (2)$$

where $c(r)$ is the cost of rewarding the target and $g(h)$ is the cost of imposing the harm.¹⁵ The functions $c(\cdot)$ and $g(\cdot)$ are assumed to be strictly increasing, continuously differentiable, and strictly convex with $c'(0) = g'(0) = 0$. The cost of providing rewards is likely to be high relative to the cost of harm. For example, a seal of approval may need to be continuously monitored or audited.

13. This aspect of the model is related to that in Dal Bo et al. (2006). Konrad and Skaperdas (1998) provide a model of extortion.

14. Dal Bo et al. (2005) consider a reputation model with a long-lived player with private information about its type playing a game with a sequence of one-period players each of which can be either sane or crazy. The probability p corresponds to the probability that a one-period player is sane.

15. Donors are assumed to provide $c(r)$ if the campaign succeeds and $g(h)$ if it fails. Uncertainty about the ability of the activist to raise the funds can be incorporated into the model. Suppose the activist can raise $c(r)$ or $g(h)$ with probability s and zero with probability $1 - s$. Then, the condition in (1) becomes

$$\pi(x_D) + sr \geq \pi(x_0) - sh.$$

The model in (1) and (2) is specific to a particular campaign; that is, the costs of providing rewards and harm could depend on the target or the activist group. The costs of rewarding and harming an industrial products firm are likely higher than for a consumer products firm, and the costs of harm can differ among targets in the same industry as well as between corporate and market campaigns. The probability p also depends on the identity of the target and its reputation in the nonmarket environment. Reputations in the nonmarket environment can change quickly. Alan Murray, writing in *The Wall Street Journal*, explained the responsiveness of the large banks to RAN's global finance campaign: "the real secret of RAN's success is that the big banks have neither the courage nor the credibility to stand up to the group. That is the price paid for three years of scandal."¹⁶ Moreover, two campaigns against targets with the same p can have different demands depending on the issue of concern to the activist as reflected in $v(\cdot)$, the current practices of the target, and the costs of conducting the campaigns.

Given the selection of a target, the activist chooses its campaign strategy to maximize (2) subject to (1). The inequality in (1) holds as an equality, because for given r and h the activist has an incentive to increase its demand to the point at which the responsive target is indifferent between conceding and not. Substituting $r = \pi(x_0) - \pi(x_D) - h$ from (1) into (2) and differentiating yields the first-order conditions for the optimal (x_D^*, h^*) :

$$p(v'(x_D^*) + c'(\pi(x_0) - \pi(x_D^*) - h^*)\pi'(x_D^*)) = 0 \quad (3)$$

$$pc'(\pi(x_0) - \pi(x_D^*) - h^*) - (1 - p)g'(h^*) = 0. \quad (4)$$

It is straight forward to show that $v(\cdot)$ concave is sufficient, but not necessary, for the second-order conditions to be satisfied.¹⁷

16. *The Wall Street Journal*, April 13, 2005. RAN had begun its campaign targeting Citigroup 2 years before the scandals became public.

17. The Hessian can be shown to be negative definite using

$$\frac{\partial^2 U}{\partial x_D^2} = p(v''(x_D^*) + c'(\pi(x_0) - \pi(x_D^*) - h^*)\pi''(x_D^*)) - c''(\pi(x_0) - \pi(x_D^*) - h^*)(\pi'(x_D^*))^2 < 0,$$

$$\frac{\partial^2 U}{\partial h^2} = -pc''(\pi(x_0) - \pi(x_D^*) - h^*) - (1 - p)g''(h^*) < 0,$$

and

$$\frac{\partial^2 U}{\partial x_D \partial h} = -pc''(\pi(x_0) - \pi(x_D^*) - h^*)\pi'(x_D^*) > 0.$$

The optimal campaign (x_D^*, r^*, h^*) satisfies (3), (4), and $r^* = \pi(x_0) - \pi(x_D^*) - h^*$, provided that the gain $G \equiv U(x_D^*, r^*, h^*) - v(x_0) \geq 0$ or

$$\begin{aligned}
 G &= p(v(x_D^*) - c(r^*)) + (1 - p)(v(x_0) - g(h^*)) - v(x_0) \\
 &= p(v(x_D^*) - v(x_0) - c(r^*)) - (1 - p)g(h^*) \geq 0.
 \end{aligned}
 \tag{5}$$

If this condition is not satisfied, the activist does not conduct a campaign and the target does not change its practices.

From the perspective of a responsive target, once it has conceded to an activist's demand and changed its practices, its profit $\pi(x_D^*) + r^* = \pi(x_0) - h^*$ is below that of its competitors, assuming otherwise identical firms. Moreover, if there are strategic effects, such as higher marginal costs, the target has a competitive disadvantage. The target then has an incentive to urge its competitors to change their practices. After Citigroup conceded to RAN's demands, CEO Charles Prince offered to call Bank of America and JP Morgan Chase, RAN's next two targets, and urge them to make similar changes in their practices. RAN accepted the offer. Bank of America quickly agreed to RAN's demand, whereas JP Morgan resisted for a year and then conceded.

The campaign (x_D^*, r^*, h^*) is more aggressive the higher the probability p the target is responsive. The campaign also becomes more negative, because the activist increases the harm, whereas the effect on the rewards is ambiguous. That is, $\frac{dh^*}{dp}$ and $\frac{dx_D^*}{dp}$ are positive.¹⁸ The greater is p the weaker is the target, and weaker targets face more aggressive campaigns in the form of a stronger threat and a higher demand. This results because the higher the probability the target is responsive to the campaign, the lower is the expected cost $(1 - p)h$ of harm and the greater is the expected gain from a campaign. The effect of p on the reward is ambiguous, because from (1) the activist has an incentive to increase the

18. The derivatives are

$$\begin{aligned}
 \frac{dh^*}{dp} &= -\frac{\frac{\partial^2 U}{\partial h \partial p} \frac{\partial^2 U}{\partial x_D^2}}{|H|} > 0 \\
 \frac{dx_D^*}{dp} &= -\frac{\frac{\partial^2 U}{\partial x_D \partial h} \frac{dh^*}{dp}}{\frac{\partial^2 U}{\partial x_D^2}} > 0,
 \end{aligned}$$

where H is the Hessian. Then,

$$\frac{dr^*}{dp} = -\pi'(x_D) \frac{dx_D^*}{dp} - \frac{dh^*}{dp}.$$

reward to allow a higher demand and to decrease the reward when the threat of harm is stronger.

The activist's utility $U(x_D^*, r^*, h^*)$ is strictly increasing in the current practices x_0 of the target, but the effect on the gain G is ambiguous. The campaign demand x_D^* is strictly increasing in x_0 , so better current practices result in a higher demand. The effect on the harm depends on the properties of $v(\cdot)$ and $\pi(\cdot)$. If both are linear, h^* is constant in x_0 ; whereas if $\pi(\cdot)$ or $v(\cdot)$ is strictly concave, h^* is decreasing in x_0 .¹⁹ If h^* is decreasing in x_0 , r^* is increasing in x_0 .

To make more specific predictions about campaigns, specific functional forms for the utility functions will be used. Let $v(x) = \gamma x$, $\pi(x) = \bar{\pi} - \eta x$, $c(r) = \alpha r^2$, and $g(h) = \beta h^2$, where the parameter η is the marginal cost to the target of conceding to the activist's demand and γ is the activist's marginal valuation of the target's practices. When rewards are difficult to provide, α is high. So, the campaign demand x_D^* is linear and increasing in the harm h^* ; that is,

$$x_D^* = x_0 + \frac{p\alpha + (1-p)\beta}{p\alpha\eta} h^*.$$

The optimal campaign is given by²⁰

$$x_D^* = x_0 + \frac{\gamma(p\alpha + (1-p)\beta)}{2\eta^2\alpha\beta(1-p)} \quad (6)$$

$$r^* = \frac{\gamma}{2\eta\alpha} \quad (7)$$

$$h^* = \frac{p\gamma}{2\eta\beta(1-p)}. \quad (8)$$

The demand x_D^* is strictly increasing in γ , p , and x_0 and strictly decreasing in α , β , and η .²¹ The example includes three cost parameters: α and β in the activist's cost function and η indexing the target's cost of conceding. Higher costs of conducting a campaign, including the cost of conceding, lead the activist to demand less, whereas the greater the

19. If $v(\cdot)$ is linear and $\pi(\cdot)$ strictly convex (and the second-order conditions are satisfied), h^* is increasing in x_0 .

20. If the activist cannot provide rewards, the harm is given by (8) and $x_D^* = \frac{p\gamma}{2\eta^2\beta(1-p)}$. If $p = 1$, the activist knows that the target will concede and hence makes an unlimited demand and backs it with an unlimited threat. Such demands and threats must, of course, be credible as considered in Section 5.

21. The change $x_D^* - x_0$ from (6) is constant in the current practices. This property is due to the linearity of $v(\cdot)$ and $\pi(\cdot)$. If $v(x) = \gamma x - x^2$, for example, then $\frac{dx_D^*}{dx_0} < 1$.

marginal benefit γ to the activist and the more likely p is the target to be responsive the higher is the demand. The reward is also increasing in the marginal value γ to the activist and decreasing in the cost parameter α and the cost to the firm of conceding. The harm is strictly increasing in γ and p and strictly decreasing in η and β . The ratio of the reward to the harm is

$$\frac{r^*}{h^*} = \frac{(1-p)\beta}{p\alpha}, \quad (9)$$

so if rewards are costly to deliver (high α), the campaign will emphasize harm relative to reward. Similarly, if the firm is believed to be responsive (high p), harm will be emphasized.

As an application of the comparative statics of the model, consider a technological advance that alters the costs of conducting a campaign. The Internet has lowered campaign costs by reducing the cost of alerting citizens to issues, mobilizing them for individual and collective action against targets, and improving the coordination of dispersed actions against a target. Suppose the technological advance allows the activist to execute its threat more efficiently and effectively. This can be represented by a decrease in the cost parameter β . Campaigns are then more aggressive (higher x_D^*) and more negative (higher h^*). The technological advance thus decreases the investment in the industry and can increase the supply of activism by increasing funding by citizens. Technological change may be one explanation for the growth of activism and for its increased impact.

The expected utility from (2) of the activist for the example is

$$\begin{aligned} U(x_D^*, r^*, h^*) &= \frac{1}{2} p\gamma(x_D^* - x_0) + \gamma x_0 \\ &= \frac{p\gamma^2(p\alpha + (1-p)\beta)}{4\eta^2\alpha\beta(1-p)} + \gamma x_0. \end{aligned} \quad (10)$$

The utility in (10) is increasing in the marginal value γ to the activist and in the responsiveness of the target, as represented by p . It is decreasing in the costs (α , β , η) of the campaign. The utility is also increasing in the current practices. The activist will conduct a campaign if and only if its gain in (5) is nonnegative, and for the example

$$\begin{aligned} G &= \frac{1}{2} p\gamma(x_D^* - x_0) \\ &= \frac{p\gamma^2(p\alpha + (1-p)\beta)}{4\eta^2\alpha\beta(1-p)} \geq 0, \end{aligned} \quad (11)$$

so the activist conducts a campaign for all parameter values. Note that the gain is independent of the current practices.

2.3 WHY ARE CAMPAIGNS NEGATIVE?

In his overview of the history of boycotts Friedman (1999) observed that campaigns usually rely on threats and negative tactics. There are many more attacks on companies than endorsements, and activists seldom demonstrate in favor of firms. The model provides four explanations for why threats are preferred to rewards. First, consider the implications for an industry whose members are targeted. The profit π^* of a target, whether it concedes or refuses to concede, is reduced by a campaign, because

$$\pi^* = \pi(x_D^*) + r^* = \pi(x_0) - h^* < \pi(x_0).$$

For the example

$$\pi^* = \pi(x_0) - \frac{p\gamma}{2\eta\beta(1-p)}. \quad (12)$$

Rewards alone ($h = 0$) would increase the profit of the target, but with harm profits are reduced because the ability to harm allows the activist to make a higher demand. Harm thus reduces the profits of targets and discourages investment in the industry. This reduces the scale of the industry and hence the practices to which the activist objects.

Second, campaigns are negative because activists select among potential targets based on their likely responsiveness p . This selection effect means that the observed campaigns are those with higher p targets. From the model the demand x_D^* and the harm h^* are increasing in p , whereas the effect on r^* is ambiguous. For the example, r^* is constant in p , and from (9) the ratio of reward to harm is decreasing in p . This implies that observed campaigns will tend to emphasize harm.

Third, harm is emphasized when rewards are costly to provide. That is, the endorsement effect may be weak, and customers may not respond to an activist's endorsement. Just as RAN does not believe that it can demonstrate to targets that a boycott harms sales, it does not believe that praise will help a target nor that other firms in the industry will change their practices in anticipation of praise. This suggests that campaigning activists may have little ability to reward a target, that is, α is high, which from (9) implies that harm is emphasized over rewards.²²

An example of rewards is a certification system. The Fair Trade movement certifies products that conform to specific environmental

22. Activist campaigns such as those of RAN may lead some firms to seek moderate NGOs with which to work in the hope of avoiding a campaign.

and human rights standards.²³ Fair Trade certification began with coffee and has been extended to a variety of products. NGOs in the fair trade movement reward participating firms by providing a seal to identify their products to consumers, but they also threaten firms. Global Exchange successfully targeted Starbucks to sell fair trade coffee. Starbucks resisted fair trade coffee because it did not believe that the coffee met the company's quality standards (Argenti, 2004). Oxfam America successfully targeted Dunkin' Donuts and Procter & Gamble to sell fair trade coffee, and the Fair Trade Organization (FTO) pressured supermarkets in Europe not to change a high price for fair trade coffee. Ultimately, as the FTO stated, "The impact of Fair Trade in the end always depends on the goodwill and loyalty of the consumer."²⁴ Paul Rice, founder and chief executive of TransFair USA, said, "It is guilt free coffee, but I would not call it that. I would call it feel-good coffee."²⁵ Bill Conerly of the National Center for Policy Analysis commented, "It's a feel-good program. I don't expect it to be a broad trend because people don't like to spend more money. I expect the impact to be trivial."²⁶ This suggests that α is high.

Fourth, as shown in Section 3 a negative campaign can induce proactive self-regulation on the part of potential targets. Although the proactive measures are not as strong as the demand the activist would make in a campaign, they enable the activist to avoid the costs of rewards or harm and to campaign against another target.

2.4 TARGET SELECTION

The activist chooses both a cause (or issue) and a target. RAN chose as its causes old growth forests, global finance, and global climate change. Its first targets in the three causes were retailers and Boise Cascade, Citigroup, and Ford, respectively. An activist prefers causes that are important (high $v(x_D) - v(x_0)$) and where it would make a difference; that is, a high demand x_D^* in its campaign. From (11) a good target for the activist is one with high valuation γ , a high probability p of responsiveness, and low costs (η, α, β) of a campaign. Easley and Lenox (2005) found that environmental activists targeted profitable firms with strong brands that were also heavy polluters.

In its global climate change campaign RAN decided to target a US automaker and chose as its target Ford rather than General Motors

23. Fair Trade can be thought of as a private institution that matches consumers with particular preferences to producers that agree to follow particular practices.

24. www.fairtrade.net.

25. *San Jose Mercury News*, April 28, 2004.

26. *San Jose Mercury News*, April 28, 2004.

(GM), which had shown greater opposition to measures to address global climate change. RAN's reasons for its choice were (1) Ford had a primary and prominent brand in the United States, whereas GM sold vehicles under a larger number of domestic brands (Chevrolet, Buick, Oldsmobile, Pontiac, Cadillac, GMC, Hummer, Saturn, and Saab). Thus, Ford's brand equity was a clearer target than GM's brands. In the notation of the model, Ford was easier to harm; that is, β was lower. (2) CEO and Chairman Bill Ford had been a supporter of the environment and was thought to be sympathetic to environmental causes. Ford, for example, had pledged to increase the fuel economy for its SUVs by 25 % by 2005. A campaign would provide Bill Ford with an opportunity to go further in embracing higher fuel economy. In the notation of the model, p was higher. Ford, however, had broken its promise by announcing that it would not meet its fuel economy goal for SUVs because of surging demand for large SUVs. (3) Ford had been targeted by other environmental activist groups, including the Bluewater Network, Global Exchange, and the Sierra Club, and multiple activist groups with the same target increased the pressure. The opportunity for cumulative harm may imply a lower β . (4) Ford had the lowest fleet fuel economy of the US automakers. This is consistent with the example with $v(\cdot)$ strictly concave as in footnote 21.

The model has implications for the level of economic activity in an industry. The profit of the target given by the right-hand side of (12) for the example is strictly decreasing in the probability p and the activist's marginal valuation γ and is strictly increasing in β and η . Activism that utilizes threats thus results in less investment in the targeted industry. That is, if the opportunity cost of the resources committed to this activity is $\bar{\pi}$, then some targets with $\pi(x_0) - h^* < \bar{\pi}$ will withdraw resources from the industry. In addition, the threat of harm lowers the profits of those firms that remain in the industry, thus making the industry less attractive to new entrants. Michael Klein, a board member of RAN said, "RAN is not out to hurt corporations. If the playing field is leveled across an industry, then corporations can still thrive and be successful."²⁷ A level, but higher cost, playing field, however, means less investment and fewer firms in the industry. Successful activism thus has a private regulation effect on an industry similar to public regulation. Lyon and John (2003) show that voluntary environmental agreements as an alternative to government regulation also result in exit from the industry.

The model is not capable of addressing several questions about targeting. For example, if the activist targets an industry, will it target

27. Baron and Yurday (2004b).

firms sequentially or simultaneously? Targeting one firm in an imperfectly competitive industry, for example, raises competitive issues. A firm has a higher cost of conceding to the extent that conceding would raise its costs and give its rivals a strategic advantage.²⁸ If the first target, however, expects that its rivals will also be targeted, then its competitive disadvantage will be short-lived. Section 3.1 considers the targeting choice among firms without considering such strategic interactions.

Strategic considerations among targets can affect the cost of conceding to the activist's demands and hence also affect the campaign itself. Consider the first target selected in an industry. If the target concedes, its costs are increased, and its competitive situation is weakened compared to other firms in the industry. It will then lose profits not only because of its higher costs but also because its market rivals will be more aggressive.²⁹ This strategic effect would be included in the cost $\pi(x_D) - \pi(x_0)$, which makes it more costly to concede. For the example, η is higher, and the campaign will be less aggressive.

Offsetting this competitive effect is the effect of concession by the first target on the campaign launched against the second target in an industry. Campaigns must be financed, and success with one target can generate more contributions for the activist organization. The increased funding then allows the activist to mount a more aggressive campaign, which then can impose higher costs of concession on the second target. When RAN targets an industry, it challenges each successive target to do more than the previous targets. The strategic disadvantage of the first target then can be offset or even reversed to a strategic advantage.

If the target fights and defeats the activist campaign, the defeat may reduce the financial contributions to the activist organization.³⁰ The campaign against the next target in the industry, if there is one, then will be less aggressive. This effect reduces the strategic gain to the first target from fighting the campaign.

2.5 VARIATION IN THE PATTERN OF ACTIVISM

The model implies variation in the pattern of activism. Variation is a function of the issue, the responsiveness of potential targets, and the costs of a campaign, which depend on both the target and the issue. One natural source of variation is between consumer products companies, such as Disney, McDonald's, Nike, and Starbucks, and

28. See Innes (2004) for a model of activist targeting with two firms competing with differentiated products.

29. This reasoning is based on a Cournot model. Innes considers strategic interactions among firms and target selection in an industry in a quite different model.

30. Fighting a campaign is considered in Section 4.

industrial products companies. Harming a consumer products company by damaging its reputation may be relatively low cost (low β) for an activist, whereas harming an industrial products company may be quite costly. The shift by activists to market campaigns against the value chain of the ultimate target, such as Boise Cascade and Weyerhaeuser, however, has lowered the cost of harming many industrial products companies.

The pattern of activism can also vary across industries. In industries, such as apparel, cosmetics, and gasoline, where it is easy for the public to participate (low α or β), activists may use more aggressive campaigns than in industries where participation is more difficult, as in pharmaceuticals or earth-moving equipment. Or, in the context of the model in Section 4, campaigns may be more successful when the public can participate than when it is more costly to do so. Friedman (1999) studied PETA campaigns and found that its animal testing campaigns against cosmetics firms were successful, whereas those against pharmaceutical companies failed.

Public participation costs may also differ among firms. Starbucks's clientele may be more responsive (lower α and β) than Dunkin Donuts's clientele. In RAN's global finance campaign, the costs of public participation may have been lower for project finance banks with large consumer banking and credit card businesses than with those with little consumer banking or credit card business. Similarly, the banks involved in scandals, such as those associated with Enron and WorldCom, could be more responsive (higher p) to an activist campaign than banks that were not involved in the scandals.

Variation can also be present within an industry. Some companies may have lower costs η of changing their practices than others. Timber companies operating in states in the northwest where state environmental regulations are stringent may have lower costs of changing their practices than timber companies operating in the south where regulations are less stringent.

Variation can also occur across activist organizations. There is a continuum of activist organizations from radical to collaborative, and those at one end of the spectrum may choose targets that are different from those at the other end. In campaigns on fair trade coffee, Global Exchange at the more radical end of the spectrum targeted Starbucks, and Oxfam America, which is closer to the other end of the continuum, targeted Procter & Gamble and Dunkin Donuts.

2.6 THE MARKET FOR ACTIVISTS

Activists must be supported by citizens, and activists could adopt different strategies. Some could solely offer rewards, some could only

use harm, and some could use both. Citizens would then support the activist that yields the greatest return for their contributions.³¹ Consider an activist that only uses rewards. For the example the equilibrium rewards are those given in (7), and the expected cost C^r is

$$C^r = \frac{p\gamma^2}{4\eta^2\alpha}.$$

The surplus G^r is analogous to (11) and can be shown to satisfy $G^r = C^r$. Consequently, the ratio of the return to the contributions is one.

The same analysis for the activist that only uses harm and the one that uses both rewards and harm yields

$$\frac{G^r}{C^r} = \frac{G^h}{C^h} = \frac{G^*}{C^*} = 1,$$

where C^h and C^* are the expected costs for activists that only use harm and that use both, respectively. The return to a contributor is thus the same for all three types of activist, so all three would be expected to be in the market. Some activists thus "cooperate" with their targets, whereas others simply use threats, whereas others such as RAN use both.

The most aggressive demands are made by the activist that uses both rewards and harm:

$$x_D^* = x_D^r + \frac{1}{\eta}h^* = x_D^h + \frac{1}{\eta}r^*,$$

where x_D^r denotes the demand by the activist that only uses rewards and x_D^h denotes the demand by the activist that only uses harm. The activist that uses both harm and rewards thus accomplishes more than the other activists but requires greater contributions.

3. PROACTIVE MEASURES BY POTENTIAL TARGETS

3.1 SELF-REGULATION

A potential target can determine from (11) how attractive it is. It then can take two types of measures in anticipation of a campaign. One is proactively to change its practices in the hope of avoiding a campaign. This will be referred to as self-regulation. Maxwell et al. (2000) found that firms reduced their toxic emissions beyond that required by public regulation, and the reductions were greater the greater the number of environmentalists in the state in which their plants were located.

31. Free-rider problems are not considered here.

The second is to increase the activist's belief that the potential target is recalcitrant.

3.1.1 SELF-REGULATION WITH A SINGLE TARGET

Consider first a proactive concession intended to preclude a campaign. The attractiveness of a proactive concession depends on whether the activist can or cannot commit to conduct a campaign once the target makes a concession. Suppose first that the activist can commit not to conduct a campaign if the potential target changes its practices sufficiently. Such a commitment could be credible because of the reputation of the activist. The activist will not conduct a campaign if the new practices \hat{x} satisfy $v(\hat{x}) \geq U(x_D^*, r^*, h^*)$ or for the example

$$\hat{x} - x_0 \geq \frac{p}{2}(x_D^* - x_0). \quad (13)$$

This implies that even for a high- p potential target the required proactive change is less than half the change that would be demanded by the activist in a campaign. The target is willing to adopt the practices \hat{x} provided that

$$\pi(\hat{x}) \geq \pi(x_0) - h^*$$

or for the example

$$\frac{h^*}{\eta} \geq \hat{x} - x_0. \quad (14)$$

The potential target thus will take proactive measures only if they are less costly than the harm from the campaign. The condition in (14) is

$$x_D^* - \frac{\gamma}{2\eta^2\alpha} \geq \hat{x},$$

$$\text{so } \hat{x} < x_D^*.$$

Combining (13) and (14) yields necessary and sufficient conditions for a proactive strategy to be adopted and a campaign forestalled:

$$x_0 + \frac{h^*}{\eta} \geq \hat{x} \geq x_0 + \frac{p}{2}(x_D^* - x_0). \quad (15)$$

An \hat{x} satisfying (15) exists if and only if

$$\frac{2-p}{1-p} \geq \frac{\beta}{\alpha}. \quad (16)$$

Consequently, if from (9) harm is emphasized over reward in the campaign, proactive measures will be observed. The left-hand side of (16) is increasing in p , so the more likely a campaign is to be successful, the larger is the set of practices that can forestall a campaign. This implies that more responsive firms are more likely to make proactive changes. The right-hand side of (16) is decreasing in α and increasing in β , so the more costly is delivering harm and the less costly are rewards the smaller is the set of practices that will forestall a campaign.

A responsive type has an incentive to take proactive measures satisfying (15). A recalcitrant type has the same incentives when (15) is satisfied, provided that it is not opposed to taking proactive measures for other reasons. Consequently, under this condition the types will pool.

If proactive measures are interpreted as corporate social performance, this analysis identifies conditions under which corporate social performance constitutes a substitute for an activist campaign. Activism and proactive corporate social performance are thus positively related. This corporate social performance is a form of self-regulation induced by the threat of activism.

If the activist cannot commit to forego a campaign against a target that makes proactive changes, a potential target faces a hold-up problem. If the potential target adopts \hat{x} , the activist acts opportunistically and launches a campaign satisfying (1) with $\pi(\hat{x})$ replacing $\pi(x_0)$. The strategic target concedes to the demand, whereas a recalcitrant target leaves \hat{x} in place.³² For the example, the incentives (r^* , h^*) are unchanged and given by (7) and (8), and the demand increases by $\hat{x} - x_0$. The profit of the target if it concedes to the activist's demand is $\pi(x_D^* + \hat{x} - x_0) + r^*$ and if it does not concede is $\pi(\hat{x}) - h^*$. Because $\hat{x} > x_0$, the potential target cannot gain by taking proactive measures. It would like to take proactive measures to forestall a campaign but, due to the hold-up problem, does not do so because the activist will still launch a campaign. Activism thus faces a commitment problem.

A reputation earned by the activist could provide the commitment required to induce proactive measures.³³ An activist gains from proactive measures, so an activist has an incentive to develop a reputation for not exploiting those potential targets that take substantial proactive measures (satisfying (13)). However, even if one activist group can commit not to target a firm that makes a proactive change, such a

32. That is, the recalcitrant target is assumed not to rescind \hat{x} out of principle or spite.

33. Maxwell, Lyon, and Hackett consider a model in which players have a fixed cost of acting, which gives rise to inaction for some parameter values. In the context of the model considered here, if the activist incurred a fixed cost associated with launching a campaign, the hold-up problem would be mitigated.

commitment need not bind another activist group that could target the firm.

3.1.2 SELF-REGULATION WITH MULTIPLE POTENTIAL TARGETS

If multiple targets are available, proactive measures could induce the activist to switch to another target that would yield a greater expected gain. Suppose there are two potential targets, but the activist has the capacity to target only one of the two.³⁴ In addition, suppose that there are no strategic interactions between the two firms. Let the utility from targeting firm 2 be denoted $U(x_{D2}^*, r_2^*, h_2^*)$, where (x_{D2}^*, r_2^*, h_2^*) denotes the optimal campaign. The activist will target firm 2 with current practices x_{02} if and only if

$$U(x_{D1}^*, r_1^*, h_1^*) + v(x_{02}) \leq v(\hat{x}_1) + U(x_{D2}^*, r_2^*, h_2^*), \quad (17)$$

where the subscript 1 denotes the first firm above, \hat{x}_1 is the proactive measures by firm 1, and $U(x_{D1}^*, r_1^*, h_1^*)$ is given in (4) for \hat{x}_1 . For the example, (17) is

$$\frac{1}{2}p_1(x_{D1}^* - x_{01}) + x_{01} - \hat{x}_1 \leq \frac{1}{2}p_2(x_{D2}^* - x_{02})$$

or

$$p_1 \frac{\gamma(p_1\alpha_1 + (1-p_1)\beta_1)}{4\eta_1^2\alpha_1\beta_1(1-p_1)} + x_{01} - \hat{x}_1 \leq p_2 \frac{\gamma(p_2\alpha_2 + (1-p_2)\beta_2)}{4\eta_2^2\alpha_2\beta_2(1-p_2)}. \quad (18)$$

Firm 1 thus can have an incentive to adopt a proactive measure \hat{x}_1 to shift an activist to an alternative target. Firm 1 will take the proactive measure if

$$\pi_1(\hat{x}_1) \geq \pi_1(x_{D1}^*) + r_1^* = \pi_1(x_{01}) - h_1^*, \quad (19)$$

which is (14). If the two potential targets have the same parameter values, there exists an \hat{x}_1 satisfying (18) and (19) for all parameter values.

Activism thus has a multiplier effect when there are multiple possible targets; that is, activism can change the behavior of firms that are not targeted as well as those that are targeted.

If both firms can take proactive measures, a competition in proactive measures can result. To show this, let the activist target firm 1 with

34. RAN, for example, has the budget capacity to conduct only three campaigns simultaneously, and it chooses to conduct those campaigns on different issues.

probability ϕ and firm 2 with probability $1 - \phi$, and assume as in the basic model in Section 2.2 that the activist can credibly commit to launch one campaign. The activist thus maximizes its expected utility EU given by

$$EU = \phi(U(x_{D1}^*, r_1^*, h_1^*) + v(\hat{x}_2)) + (1 - \phi)(v(\hat{x}_1) + U(x_{D2}^*, r_2^*, h_2^*)). \quad (20)$$

Each firm i has an incentive to take proactive measures as in (18). This incentive persists provided that the measures are less than the constraint in (19). That is, the firms will compete to avoid a campaign, resulting in a race to the top. The equilibrium then is that both targets take proactive measures to the point that (19) is binding for one firm. This is equivalent to the activist conducting a second-price auction for the opportunity to avoid a campaign.

Suppose the two firms are identical, and \bar{x} is the maximum of the set of practices that satisfy (19). The firms will compete to avoid being the target to the point at which $\hat{x}_i = \bar{x}$, $i = 1, 2$, or if the firms are identical,³⁵

$$\hat{x}_1 = \hat{x}_2 = x_0 + \frac{p\gamma}{2\eta^2\beta(1-p)} > x_D^*,$$

which implies that

$$\hat{x}_1 + \hat{x}_2 \geq x_D^* \iff x_0 + \frac{\gamma(p\alpha - \beta(1-p))}{2\eta^2\alpha\beta(1-p)} \geq 0.$$

A sufficient but not necessary condition for the right inequality to be satisfied is that harm is emphasized over reward in the campaign as in the discussion of (9). The race to the top then leads to greater aggregate change than if the activist were simply to launch a campaign against

35. To show that this is an equilibrium, note that from (20) firm 1 will be targeted unless

$$v(\hat{x}_1) \geq U(x_{D1}^*, r_1^*, h_1^*) + v(\hat{x}_2) - U(x_{D2}^*, r_2^*, h_2^*).$$

Firm 1 will choose such an \hat{x}_1 if (14) is satisfied. Similarly, firm 2 will be targeted unless

$$v(\hat{x}_2) \geq U(x_{D2}^*, r_2^*, h_2^*) + v(\hat{x}_1) - U(x_{D1}^*, r_1^*, h_1^*)$$

and $\hat{x}_2 \leq \frac{h_2^*}{\eta}$. Given \hat{x}_2 , firm 1 will increase its proactive measures provided that $\hat{x}_1 \leq \frac{h_1^*}{\eta}$, and given \hat{x}_1 , firm 2 will increase its proactive measures provided that $\hat{x}_2 \leq \frac{h_2^*}{\eta}$. The equilibrium thus is

$$\hat{x}_1 = \hat{x}_2 = \bar{x} \equiv \min \left\{ \frac{h_1^*}{\eta}, \frac{h_2^*}{\eta} \right\}.$$

If the firms are identical, $\bar{x} = x_0 + \frac{p\gamma}{2\eta^2\beta(1-p)}$.

one firm in the absence of proactive measures. Note that this is the case regardless of whether the activist can commit not to target a proactive firm.

When the activist can induce a competition in proactive measures, what strategy do potential targets adopt? Collective action by an industry is one response. The firms in the industry have an incentive to act collectively to avoid being caught in a race to the top. The US forest products industry did so in establishing the Sustainable Forest Initiative (SFI) which sets standards for forest stewardship. Over 90 percent of the industry members participate in SFI. Collective action for the industry was easy because the firms had an already-established industry association. Similarly, during RAN's global finance campaign Citigroup and three other banks developed the Equator Principles to guide the financing of projects in ecologically sensitive areas. Both SFI and Equator Principles restrict a race to the top and can be thought of as a collective move to the middle.

3.2 TARGET REPUTATION

The campaign depends on the beliefs p about whether the target will concede to the activist's demand. For example, companies that position themselves as socially responsible can make good targets on some issues because they have revealed themselves as soft and responsive. Starbucks' agreement to sell Fair Trade coffee may be an example. Argenti (2004) concluded that "truly socially responsible companies are actually more likely to be attacked by activist NGOs than those that are not. . . . Our interviews with Global Exchange suggested that Starbucks was a better target for the fair trade issue because of its emphasis on social responsibility, as opposed to a larger company without a socially responsible bent."

A potential target may be able to influence those beliefs through its actions. For example, the potential target may establish a reputation for not responding to coercion, challenging government regulations, and fighting lawsuits rather than settling. These actions may have different costs for different potential targets, so the strategies chosen by potential targets can reveal information about their type. This also means that one potential target can emulate another, albeit at a different cost.

To consider target reputation-building strategies in the context of the model, suppose that a potential target can be either hard (H) or soft (S). A target of type j has a probability p_j , $j = H, S$, of being responsive to a campaign, where $0 < p_H < p_S < 1$. Suppose that the prior probability that the potential target is H is ρ_0 , so the ex ante probability p_0 that the target will concede is

$$p_o = \rho_o p_H + (1 - \rho_o) p_S.$$

Reputations are built on a record of actions. A reputation for being hard could be built from signals such as aggressively fighting shareholder resolutions, filing a lawsuit against the EPA on a regulatory matter, and challenging activists. In the oil industry, signals could include actively supporting energy legislation that benefits the industry and by supporting the Global Climate Coalition or Arctic Power, which opposes strong action against global warming and supports opening the Arctic National Wildlife Refuge for oil exploration, respectively. In contrast, BP withdrew from both organizations. A reputation for being soft could also result from corporate social responsibility policies.

Suppose that the potential target can send one of two public signals $m_j, j = H, S$, that are consistent with a hard- and soft-type target, respectively. Let $\sigma_H(j), j = H, S$, be the probability that type j sends the signal m_H , where $1 - \sigma_H(j)$ is the probability that m_S is sent. Suppose that type H has a low cost of sending m_H , because it would be taking the supporting actions anyway, so $\sigma_H(H) = 1$. In addition, suppose that type S has a high cost of sending m_H , so $\sigma_H(S)$ can be less than 1. The posterior probability $\rho(m_H)$ that the target is H given m_H is

$$\rho(m_H) = \frac{\rho_o}{\rho_o + (1 - \rho_o)\sigma_H(S)},$$

and the posterior probability given m_S is $\rho(m_S) = 0$. The activist's belief $p(m)$ about whether the target will concede is then $p(m_S) = p_S$ and

$$p(m_H) = \rho(m_H)p_H + (1 - \rho(m_H))p_S \in [p_H, p_S].$$

The activist chooses a campaign (x_{Dj}, r_j, h_j) corresponding to $p(m_j)$ when $m_j, j = S, H$, is received. When $m_S(m_H)$ is received, the activist chooses a more (less) aggressive campaign. That is, if it sends m_S , then $p(m_S) = p_S$, so from Section 2.2 the soft firm faces an aggressive campaign. A soft firm S thus has an incentive to send the costly signal m_H so as to avoid the more aggressive campaign. The soft firm is forced to signal m_H by the hard firm's willingness to signal m_H . The optimal signaling strategy $\sigma_H^*(S)$ satisfies

$$\begin{aligned} \sigma_H^*(S) \in \arg \max_{\sigma_H(S)} & \sigma_H(S)(\pi(x_0) - h_{p(m_H)}^*) \\ & + (1 - \sigma_H(S))(\pi(x_0) - h_{p(m_S)}^*) - c(\sigma_H(S)), \end{aligned}$$

where $h_{p(m)}^*$, $m \in \{m_H, m_S\}$, is the harm in the campaign corresponding to the message m . The first-order condition is³⁶

$$\frac{\gamma}{2\eta\beta} \left(\frac{p_S}{1-p_S} - \frac{p(m_H)}{1-p(m_H)} \right) - c'(\sigma_H^*(S)) = 0,$$

provided that $\sigma_H^*(S) < 1$. The strategy $\sigma_H^*(S)$ is increasing in γ and p_S and decreasing in η and β (because $h_{p(m)}^*$ is decreasing in η and β). Less aggressive campaigns result for S if it sends m_H than if it sends m_S , but the campaign given m_H is more aggressive than it would have been based on prior information.

The opportunity for a target to develop a reputation thus leads to actions (signals) that may be contrary to the interests of the activist. Activism thus can have perverse effects by encouraging soft types to act hard by taking the actions corresponding to m_H . That is, potential targets may aggressively oppose threats from both private and public politics so as to signal that they are hard.

4. CONTESTING THE CAMPAIGN

4.1 CAMPAIGN SUCCESS OR FAILURE

In the basic model the activist chooses a campaign such that the responsive target concedes. The target has no reason to resist because the harm will be delivered with certainty. Not all campaigns, however, draw sufficient support to be successful, and a target may gain from delaying action to determine whether the campaign will be successful. Moreover, the target may be able to counter the campaign and reduce its likelihood of success. A target may, for example, provide information to the public or successfully manage its reputation with its stakeholders. When targeted by RAN, Weyerhaeuser used its internal newsletter to employees to discuss the campaign and the company's forest stewardship programs. The objectives were to strengthen employee morale and solidify their support. A target may also communicate with customers or other elements of its value chain to shore up their support. This section considers a variation of the basic model in which the success of the campaign is endogenous to the strategies of the activist and the target.

The activist moves first by choosing its campaign as in the basic model. The target then can concede immediately or resist the campaign. Resisting the campaign could take a number of forms such as information provision and reputation management, but instead of modeling each possible strategy in detail, resistance or fighting will simply be

36. The first term is positive for $\sigma_H(S) < 1$, because $p_S > p(m_H)$.

represented by its intensity $f \geq 0$. Let $k(f)$ be the cost of fighting, where the cost function is assumed to be increasing and convex. The success of the campaign depends on the harm h and the fight f , and let the probability q of success be given by³⁷

$$q = \frac{\theta h}{\theta h + f}, \quad (21)$$

where $\theta \in (0, \infty)$ indexes the public's sympathy or support for the campaign. For example, if the campaign includes a boycott, θ could depend on the switching costs for consumers; that is, high switching costs correspond to low θ . The appeal θ could also be correlated with the cost of delivering harm; for example, θ and β could be negatively correlated.

If the target chooses not to fight ($f = 0$), the campaign succeeds in delivering harm with probability $q = 1$. If the target fights ($f > 0$), with probability $1 - q$ the target is able to negate the harm in the campaign. A campaign has a planned duration normalized to 1, and a target that chooses to fight does so at time 0. A fight is assumed to last for a time $\delta \in [0, 1)$ after which the outcome is realized according to (21). During a fight the harm is h , and if the campaign succeeds and the target does not concede at that point, the remaining harm $(1 - \delta)h$ is incurred. If the target concedes when the campaign succeeds, the remaining harm is avoided, and the reward is $(1 - \delta)r$. If the campaign fails because the target is able to negate the harm, the target incurs no harm for the $1 - \delta$ period and is assumed to maintain its current practices x_0 . The activist expends $g(h)$ if it loses the fight, and $\delta g(h) + (1 - \delta)c(r)$ if it wins.

4.2 OPPORTUNISTIC BEHAVIOR

In this section, the activist is assumed to act opportunistically in the event that it wins the fight at time $1 - \delta$. That is, if it wins the fight, it makes the most aggressive demand it can, and that demand satisfies (1). Assume initially that the campaign is chosen such that the target will concede if the campaign is successful. The responsive target will fight according to

$$f^* \in \arg \max_{f \in [0, \infty)} \hat{\pi} = \delta(\pi(x_0) - h) + (1 - \delta)[q(\pi(x_D) + r) + (1 - q)\pi(x_0)] - k(f). \quad (22)$$

Substituting from (1) yields

37. Maxwell, Lyon, and Hackett (2000) consider a model in which consumers and an industry can influence through public politics a government regulation, but they assume that the marginal influence is independent of the strategy of the opposition. Consumers and the industry thus do not directly compete.

$$f^* \in \arg \max_{f \in [0, \infty)} \hat{\pi} = \pi(x_0) - (q + (1 - q)\delta)h - k(f). \quad (23)$$

The expected profit of the recalcitrant type is also given in (23), so both types of the target choose the same fight. The target's profit $\hat{\pi}$ in (23) is decreasing in δ , so the target prefers to resolve the campaign as quickly as possible.

The first-order condition is

$$\frac{(1 - \delta)\theta h^2}{(\theta h + f^*)^2} - k'(f^*) = 0. \quad (24)$$

The fight f^* is chosen in response only to the harm component of the campaign, and the response function is increasing in h ; that is,

$$\frac{df^*}{dh} = \frac{\frac{2(1 - \delta)\theta h f^*}{(\theta h + f^*)^3}}{\frac{2(1 - \delta)\theta h^2}{(\theta h + f^*)^3} + k''(f^*)} > 0.$$

The fight f is decreasing in δ , because a higher δ implies that less of the harm can be negated by fighting the campaign.

The fight f^* also depends on the public's responsiveness θ to the campaign, and

$$\frac{df^*}{d\theta} = \frac{(1 - \delta)h^2(1 - 2q^*)}{\frac{2(1 - \delta)\theta h^2}{\theta h + f^*} + k''(f^*)(\theta h + f^*)^2}.$$

The fight f^* is increasing (decreasing) in θ as $f^* > (<)h\theta$ or equivalently as $q^* < (>)\frac{1}{2}$, where $q^* \equiv \frac{\theta h}{\theta h + f^*}$. If the campaign is more likely to fail than to succeed, the target fights more intensely as the public is more responsive to the campaign, but if the campaign is likely to succeed ($q^* > \frac{1}{2}$), the target fights less intensely. If the activist can choose its issue or cause in response to its public responsiveness θ , it will choose a cause with a high θ . The subsequent dynamics of the campaign thus depend on the cause.

In lieu of fighting the target can concede at the time the campaign is launched. The target will concede rather than fight if

$$\pi(x_D) + r \geq \pi(x_0) - (q^* + (1 - q^*)\delta)h - k(f^*). \quad (25)$$

Strict concavity of $\hat{\pi}$ in (23) implies

$$\begin{aligned} &\pi(x_0) - (q^* + (1 - q^*)\delta)h - k(f^*) \\ &> [\pi(x_0) - (q + (1 - q)\delta)h - k(f)]|_{f=0} = \pi(x_0) - h. \end{aligned} \quad (26)$$

The inequality in (1) and (26) thus imply that (25) is not satisfied, so the target does not concede. Consequently, the target will fight when the campaign satisfies (25) as an equality. Fighting by the target thus occurs in equilibrium when the activist will act opportunistically if the campaign succeeds.

As an example, let $k(f) = kf$ in which case

$$f^* = \theta h \left(\left(\frac{1 - \delta}{\theta k} \right)^{\frac{1}{2}} - 1 \right),$$

provided that $\frac{1 - \delta}{\theta k} \geq 1$. The fight f^* is increasing in h and θ and decreasing in the marginal cost k . The target will fight if (25) is not satisfied, which is equivalent to $\frac{1 - \delta}{\theta k} > 1$. Then, the target will not concede initially. The probability q^* that the campaign succeeds is then given by

$$q^* = \left(\frac{\theta k}{1 - \delta} \right)^{\frac{1}{2}} < 1. \tag{27}$$

This is independent of h , because f^* is linear in h for the example. As expected, an increase in the marginal cost of fighting, an increase in the public responsiveness θ , or a long delay in resolution of the contest increases the probability of a successful campaign.

The activist's expected utility U_A is

$$\begin{aligned} U_A &= \delta(v(x_0) - g(h)) + (1 - \delta)[q^*p(v(x_D) - c(r)) \\ &\quad + (1 - q^*p)(v(x_0) - g(h))] \\ &= (1 - \delta)pq^*(v(x_D) - c(r)) + (1 - (1 - \delta)pq^*)(v(x_0) - g(h)). \end{aligned} \tag{28}$$

When (1) is binding, the campaign satisfies first-order conditions corresponding to (3) and (4):

$$(1 - \delta)pq^*(v'(x_D^*) + c'(\pi(x_0) - \pi(x_D^*) - h^*)\pi'(x_D^*)) = 0 \tag{29}$$

$$\begin{aligned} (1 - \delta)pq^*c'(\pi(x_0) - \pi(x_D^*) - h^*) - (1 - (1 - \delta)pq^*)g'(h^*) \\ + (1 - \delta)\frac{\partial q^*}{\partial h}p[v(x_D^*) - c(\pi(x_0) - \pi(x_D^*) - h^*) - v(x_0) + g(h^*)] = 0. \end{aligned} \tag{30}$$

If the probability of success q^* were exogenous, (29) and (30) would be identical to (3) and (4) with $(1 - \delta)pq^*$ replacing p .

When the probability q^* of success for the activist is endogenous, it is strictly increasing in h if $k(\cdot)$ is strictly convex and constant if $k(\cdot)$ is linear. To show this, the first-order condition in (24) can be rewritten as

$$q^* = \left(\frac{\theta}{1-\delta} \right)^{\frac{1}{2}} (k'(f^*))^{\frac{1}{2}}.$$

Differentiating yields

$$\frac{dq^*}{dh} = \frac{1}{2} \left(\frac{\theta}{1-\delta} \right)^{\frac{1}{2}} (k'(f^*))^{-\frac{1}{2}} k''(f^*) \frac{df^*}{dh}, \quad (31)$$

which for $k(\cdot)$ linear equals zero. The result in (31) can be used to characterize the elasticity ϵ_f of the response function f^* . Differentiating $q^* = \frac{\theta h}{\theta h + f^*}$ yields

$$\frac{dq^*}{dh} = \frac{\theta f^*}{(\theta h + f^*)^2} (1 - \epsilon_h^*), \quad (32)$$

where $\epsilon_h^* \equiv \frac{h}{f^*} \frac{df^*}{dh}$. From (31), $\epsilon_h^* < 1$ if $k(\cdot)$ is strictly convex, and if $k(\cdot)$ is linear as in the example, $\epsilon_h^* = 1$. The target's response is inelastic when it contests the campaign.

The probability q^* of success is increasing in the public support θ for the activist's cause under a number of sufficient conditions. If the elasticity $\epsilon_\theta^* \equiv \frac{\theta}{f^*} \frac{df^*}{d\theta}$ is less than one, which is the case when $q^* > \bar{q} < \frac{1}{2}$, where \bar{q} is the probability corresponding to $\epsilon_\theta^* = 1$, greater public support results in a higher probability of campaign success. Conversely, a small increase in public support could lead the target to fight harder, and the probability of success would decrease. The probability of success is increasing in θ if $k(f)$ is linear or is strictly convex and $q^* \leq \frac{1}{2}$.

In addition, if $k(f)$ is linear, the equilibrium campaign is given by (1), (3), and (4) with $(1-\delta)q^*p$ replacing p . Because $(1-\delta)q^*p < p$, the campaign demand is less aggressive (x_D^* lower) and less negative (h^* lower) when fighting is possible. This results because campaigns are less aggressive the more likely the target is to successfully contest the campaign. Responsive firms (high p) remain the best targets for the activist.

For $k(f)$ linear the basic model presented in Section 2.2 can be re-interpreted with q^* as the probability of success when the target fights the campaign. That is, for the model in this section, let $p = 1$ and $\delta = 0$, so the probability $(1-\delta)q^*p$ of a successful campaign equals q^* , a constant.

4.3 COMMITMENT NOT TO ACT OPPORTUNISTICALLY

If the activist can commit not to act opportunistically in light of a successful campaign, it will not drive the demand up to satisfy (1) if the campaign succeeds. The activist then chooses a campaign that

avoids fighting. If it were to fight the campaign, the expected profit of the responsive type would be

$$\pi^o = \delta(\pi(x_0) - h) + (1 - \delta)[q^o(\pi(x_D) + r) + (1 - q^o)\pi(x_0)] - k(f^o), \quad (33)$$

where f^o is the optimal fight and $q^o = \frac{\theta h}{\theta h + f^o}$. The optimal fight f^o for the responsive type satisfies

$$\frac{(1 - \delta)\theta h}{(\theta h + f^o)^2}(\pi(x_0) - \pi(x_D) - r) - k'(f^o) = 0$$

and is decreasing in the reward and the current practices and is increasing in the harm and the demand. A more aggressive campaign thus results in stronger opposition to the campaign, but because a strict inequality holds in (1), $\pi(x_0) - \pi(x_D) - r < h$, so $f^o > f^*$. The responsive type thus fights less hard compared to the case in which the activist cannot commit. The recalcitrant type fights the campaign rather than conceding, and its optimal fight is f^* given in (24), so the recalcitrant type fights harder than does the responsive type.

For the example in which $k(f)$ is linear, the fight is

$$f^o = \theta h \left(\left(\frac{1 - \delta}{\theta k} \right)^{\frac{1}{2}} \left(\frac{\pi(x_0) - \pi(x_D) - r}{h} \right)^{\frac{1}{2}} - 1 \right),$$

and the probability of success is

$$q^o = \left(\frac{\theta k}{1 - \delta} \right)^{\frac{1}{2}} \left(\frac{h}{\pi(x_0) - \pi(x_D) - r} \right)^{\frac{1}{2}},$$

so $f^o = \theta h \frac{1 - q^o}{q^o}$.

The responsive type concedes rather than fights if $\pi(x_D) + r$ is at least as great as π^o in (33) or

$$\pi(x_D) + r \geq \pi(x_0) - \frac{\delta h + k(f^o)}{1 - q^o(1 - \delta)}. \quad (34)$$

The optimal campaign (x_D^o, r^o, h^o) maximizes the activist's expected utility subject to the constraint in (34).³⁸ For the example, the optimal campaign has $r^o = r^*$ as given in (7), and the probability q^o of winning satisfies

$$q^o = \frac{\theta k}{\delta - \theta k} \left(\left(\frac{\delta(1 - \theta k)}{\theta k(1 - \delta)} \right)^{\frac{1}{2}} - 1 \right).$$

38. Note that regardless of whether the activist can commit, the recalcitrant type does not concede even when the activist wins the contest.

The probability q^o depends only on θk and δ and is strictly increasing in θk with $q^o = 1$ if $\theta k = \frac{1}{2}(1 + \sqrt{1 - 4\delta(1 - \delta)})$ and $q^o = 0$ if $\theta k = 0$. The campaign demand is

$$x_D^o = x_0 + \frac{\gamma}{2\alpha\eta^2} + \frac{\delta q^o + \theta k(1 - q^o)}{\eta q^o(1 - (1 - \delta)q^o)}h.$$

The demand is linear in the harm as in the model in Section 2.2. The harm is given by

$$h^o = \frac{1}{2\beta(1 - p)(q^o)^2(1 - \delta)} \left[\frac{p\gamma\theta k}{\eta} + \lambda^o(\delta(1 - \delta)(q^o)^2 - \theta k(1 - \delta)(1 - q^o)^2 - \delta) \right],$$

where λ^o is the multiplier on the constraint in (34).

Intuition suggests that the campaign is less aggressive with commitment than without commitment. This can be verified for the case in which the cost of fighting is linear. Equalities in (1) and (34) imply that

$$\pi(x_0) = \pi(x_D^*) + r^* + h^* = \pi(x_D^o) + r^o + h^o - \frac{(1 - q^o)(1 - \delta)h^o - k(f^o)}{1 - q^o(1 - \delta)}.$$

Then, (26) implies that the last two terms on the right are positive, so

$$\pi(x_D^*) + r^* + h^* > \pi(x_D^o) + r^o + h^o.$$

The campaign is thus less aggressive when the activist can commit not to exploit a successful campaign. This is necessary to induce the responsive target to accept the demand rather than fight.

5. ACTIVISM AND CREDIBILITY

5.1 CREDIBILITY AND COMMITMENT

In the previous sections the target was assumed to view the campaign as credible, but campaign rewards are difficult to demonstrate, and the threat of harm must be backed by the capacity to deliver it. Campaigns require credibility, and credibility depends largely on the reputation of the activist organization, which is built on past actions. An important asymmetry between activists and most firms is that activists are typically engaged in many more campaigns than are its targets. This suggests that

it is easier for activists to build and maintain reputations compared to these firms that are only infrequently targeted.³⁹ Those reputations then can provide credibility for the promise of rewards and the threat of harm, as considered in Section 5.2.

A second facet of activist reputation is the ability to raise the funds to cover the cost of carrying out the campaign. Before launching a campaign, RAN expects a campaign to last 3–5 years and cost \$1 million a year. RAN also plans on no more than three campaigns at a time, given its annual budget of between \$2.5 and \$3 million. Campaign success strengthens an activist's reputation and increase contributions from citizens.

Some citizens have strong preferences for supporting activist organizations. Some have an aversion to the tactics of radical activists and are willing to support, for example, the Nature Conservancy or Environmental Defense but not RAN or Greenpeace. Activists communicate with potential contributors via the news media through its coverage of campaign activities and increasingly via the Internet. Little is known about the market for contributions in private politics, but what is evident is that contributions to these groups are substantial.⁴⁰

A third facet of activist reputation is the ability to choose campaigns that will attract sufficient public interest to deliver the rewards or harm. As indicated in Section 4, one aspect of this is the extent of public support for the issue on which the campaign is based. Some issues, such as pollution, have been supported by public sentiment, whereas others, such as costly measures to address global climate change, have drawn only modest public support in the United States.

A fourth facet of activist reputation is how committed the individual activists are. RAN has proven to be quite committed, as evidenced by its 8-year campaign against Mitsubishi Electric and Mitsubishi Motors on the issue of the harvesting of tropical rainforests, even though it was evident early in the campaign that the prospects of significant change were slight. The union UNITE demonstrated commitment in the campaign to improve working conditions and wages in factories supplying the apparel and footwear industries. Activist groups that are unable to demonstrate credible commitment are likely to wither away.

39. The validity of this statement can depend on the firm and the industry. Large firms with a strong brand, such as McDonald's and Wal-Mart, face many activist campaigns. Similarly, firms that operate in industries, for example, tobacco or alcohol, with high levels of activism, however, may find it advantageous to develop reputations for toughness.

40. RAN does not accept contributions from corporations.

5.2 REPETITION

In the one-period model considered above, the activist has an incentive to shirk on the delivery of rewards and harm, particularly when a demand is rejected because the activist knows that the target is recalcitrant. The incentive to shirk may be mitigated, however, if the activist anticipates future campaigns. Suppose the activist is infinitely-lived and plays an infinite sequence of identical one-period targets. Can the equilibrium in the one-period model with commitment in Section 2.2 be supported as an equilibrium in the infinitely repeated game in the absence of commitment? That is, can repetition eliminate the incentive for the activist to shirk on its promises? The analysis in this section thus focuses on whether repetition can support an equilibrium in which (i) the campaign is (x_D^*, r^*, h^*) in each period, (ii) responsive targets concede, (iii) recalcitrant targets resist, (iv) the activist delivers r^* when a target concedes, and (v) the activist delivers h^* when a target rejects the demand. A Markov perfect equilibrium is sought, where the states are n that the activist has never shirked and s that it has shirked at least once.⁴¹ Each target is assumed to know the state at the beginning of the period in which it is targeted.

Suppose that all future targets believe that if the activist shirks on either delivering rewards or harm, it will shirk on both in every period in the future. Then, future targets will all reject the demand x_D^* . The value function W^s of the activist is then

$$W^s = \frac{1}{1 - \mu} v(x_0),$$

where $\mu \in (0, 1)$ is the discount factor. If the activist has never shirked, its value function W^n is

$$W^n = \frac{1}{1 - \mu} [p(v(x_D^*) - c(r^*)) + (1 - p)(v(x_0) - g(h^*))].$$

Consider the state n and a target that has rejected the demand x_D^* . If the activist delivers the harm h^* , its utility is

$$-g(h^*) + \frac{\mu}{1 - \mu} W^n.$$

41. The analysis does not characterize the set of campaigns that can be supported as Markov perfect equilibria nor other equilibria that satisfy the weaker subgame perfect equilibrium conditions, which would allow punishment strategies.

If it shirks, its utility is $\frac{\mu}{1-\mu} W^s$. Then, the activist does not shirk on the delivery of harm if

$$v(x_D^*) - v(x_0) - c(r^*) + g(h^*) \geq \frac{g(h^*)}{\mu p}. \tag{35}$$

Next, consider the state n and a target that has accepted the demand x_D^* . If the activist delivers the reward, its utility is

$$-c(r^*) + \frac{\mu}{1-\mu} W^n,$$

and if it shirks, its utility is $\frac{\mu}{1-\mu} W^s$. The activist does not shirk on providing the rewards if

$$v(x_D^*) - v(x_0) - c(r^*) + g(h^*) \geq \frac{g(h^*)}{p} + \frac{1-\mu}{p\mu} c(r^*). \tag{36}$$

If these conditions are satisfied, the campaign characterized in Section 2.2 can be implemented. For the example, the conditions in (35) and (36) require, respectively,

$$\mu \geq \frac{\alpha p}{(1-p)^2 \beta + (2-p) p \alpha} < 1 \tag{37}$$

and

$$\mu \geq \frac{\beta(1-p)}{(1+p)(1-p)\beta + p^2 \alpha} < 1. \tag{38}$$

Activists with a long time horizon (high μ) thus can have incentives to provide the promised rewards and deliver on threats of harm provided that the probability of a responsive target is not too high.⁴² An activist with a long horizon thus can make credible demands, promises, and threats, but they must be fulfilled with each of its targets.

As $p \rightarrow 1$, however, the bound in (37) goes to 1, and the bound in (38) goes to 0. Consequently, for any $\mu < 1$ there exists a \bar{p} such that for $p > \bar{p}$ the activist has an incentive to shirk on the delivery of harm. This is evident from (6) and (8), because as $p \rightarrow 1$ the demand and the harm are unbounded. Consequently, targets with sufficiently high p would not incur the campaign (x_D^*, r^*, h^*) because the activist would have an

42. For example, if $p = \frac{1}{2}$,

$$\mu \geq \max \left\{ \frac{2}{3 + \frac{\beta}{\alpha}}, \frac{2}{3 + \frac{\alpha}{\beta}} \right\} < 1.$$

incentive to shirk on the harm. This results because the harm and the cost increases in p . For the example, from (8) h^* is strictly convex in p , so for some p the activist will shirk. This has two implications. First, firms with high p can avoid a campaign (x_D^*, r^*, h^*) because the activist cannot credibly commit not to shirk on the delivery of rewards or harm. This means that either the activist would choose a less aggressive campaign such that it would not shirk or it would target a firm with a lower p . Second, in contrast to Section 3.2, when p is sufficiently high, a potential target that is hard may have an incentive to signal that it is soft.

6. SUMMARY OF RESULTS

This section summarizes the principal results from the preceding sections.

1. When its campaign is credible, an activist prefers an issue with high value and strong public support and a target that is responsive to a campaign, for which the cost of a campaign is low, and the cost of fighting is high.
2. The campaign is more aggressive and more negative the weaker (more responsive) the target. For the example, the activist's demand is more aggressive the more important is the issue, the more responsive is the target, and the lower the marginal costs of conducting the campaign.
3. An activist prefers harm to reward because harm decreases investment in the targeted activity, whereas rewards alone can increase investment. Selection among potential targets leads to more negative campaigns, and harm is emphasized when rewards are costly to deliver.
4. Activists that only provide rewards, only provide harm, and provide both can be present in the market for activism.
5. An activist has an incentive through repetition to follow through on its campaign promises of reward and harm and for not exploiting targets that accept its demands.
6. A potential target can forestall a campaign through self-regulation by changing its practices proactively but only if the activist can commit not to subsequently launch a campaign or if the proactive change shifts the activist to an alternative target. Self-regulation is plagued by a hold-up problem.
7. With multiple potential targets the activist can generate a race to the top in proactive measures. This creates an incentive for an industry to act collectively.

8. A potential target may develop a reputation for toughness to forestall a campaign, and the incentive to do so is strengthened by a moral hazard problem associated with revelation of its type. Conversely, a potential target that reveals itself as responsive or soft will be a more attractive target and campaigns will be more aggressive in their demands and threats. Potential targets thus have an incentive to signal that they are tough using both public and private politics strategies.
9. In an infinitely-repeated game the activist can implement the optimal single-period campaign and has no incentive to shirk on the delivery of rewards and harm if its horizon is sufficiently long. For any given discount factor, however, the activist has an incentive to shirk on the delivery of harm in the optimal single-period campaign if the probability of responsiveness is sufficiently high. Consequently, firms that are highly likely to be targets will not incur the single-period optimal campaign.
10. If a campaign can be contested and the activist cannot commit to exploit a successful campaign, the target fights on the equilibrium path of play. If the activist can commit not to exploit a successful campaign, a responsive target concedes immediately and a recalcitrant target fights. When the cost of fighting is linear, the campaign is less aggressive when the activist can commit not to exploit a successful campaign.

7. CONCLUSION

Activism targeting firms and markets has increased substantially in recent years and has become an important component of the nonmarket environment of many firms and industries. Activists are strategic, typically deploying well-focused strategies centering on a particular issue, target, and practice. Entry into the activism industry is easy and technological change such as the Internet has shifted the supply curve of activism outward. In addition, activists are increasingly turning to private politics to advance their agenda. In part this is motivated by their lack of success in public arenas, and in part by the increasing importance of multinational corporations in global economies.

Viewing the interaction between activists and firms as a form of nonmarket competition, this paper focused on the strategic interactions between the parties, ranging from targeting strategies to proactive measure such as self-regulation or investments in socially responsible business practices. The model showed that strategic interactions play an important role in all aspects of a campaign. This has important

consequences for empirical research. For example, once targeting is modeled as a strategic choice, empirical studies of campaign success or impact need to account for possible selection bias. The same is true if self-regulation or corporate social responsibility are understood as proactive strategies to lower the probability of becoming a target in an activist campaign. Unfortunately, few systematic empirical studies of activist campaigns are available. The model presented here identifies data to be collected and provides predictions to be tested.

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