

5 October 2021

Chorus Limited (CNU)

The company will hold its Annual Shareholders Meeting at **12.00pm Wednesday 27 October 2021**

It will be a virtual meeting. You can join the meeting at

<https://apps.online.computershare.com/MeetingsShareholderWeb/FindMeeting?Country=NZ>

Company Overview

Chorus is a provider of telecommunications infrastructure. The company was demerged from Telecom New Zealand in 2011 as a condition of winning the majority of contracts for the Governments Ultra-Fast Broadband Initiative. It is the owner of the majority of telephone lines and exchange equipment and responsible for building approximately 75% of the new fibre optic network.

In November 2019 it completed UFB1 the first stage rollout to 28 major towns and cities. The second stage rollout UFB2 to 150,000 homes and businesses will be completed by the end of 2022. Fixed line connections are 1.34 million down 75,000, broadband connections are 1.18 million down 26,000 with 871,000 fibre connections up 120,000 reflecting the move from fixed line and the increase in fibre connections. Fibre uptake is 65% and the target is 1 million fibre connections in 2022.

Current Strategy

The company's strategy is to build and manage an open access internet network, rolling out ultra-fast broadband to allow phone and broadband providers offer innovative products and services to their customers.

Key

The following sections calculate an objective rating against criteria contained within NZSA policies.

Colour	Meaning
G	Strong adherence to NZSA policies
A	Part adherence or a lack of disclosure as to adherence with NZSA policies
R	A clear gap in expectations compared with NZSA policies
n/a	Not applicable for the company

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Governance

NZSA assessment against its key policy criteria is summarised below:

Policy Theme	Assessment	Notes
Directors Fees	G	Excellent disclosure.
Director share ownership	G	Whilst is not mandatory Directors are encouraged to own shares.
Executive Remuneration	G	See comments below.
Golden parachutes/handshakes	A	NZSA expects disclosure around whether these are similar payments are offered. Following discussion, NZSA is comfortable with the company's position.
Director Independence	G	Good disclosure.
Board Composition	A	See comments below.
Director Tenure	G	See comments below.
ASM Format	G	Virtual Meeting only due to Covid uncertainty
Company Sec independence	G	Generally good disclosure but not disclosed if a profit-based incentive is paid.

Executive Remuneration: NZSA appreciates the comprehensive disclosure made by Chorus in relation to executive remuneration.

The company discloses the four key 'measurement groups', their weightings and their targets associated with the short-term incentive (STI) scheme applicable to the CEO and company executives. The company does not disclose the level of achievement for each measurement group as part of the Remuneration Report, however, key metrics can be found elsewhere in the Report.

Chorus also discloses the core metric – total shareholder return – that forms the basis for its long-term incentive scheme (LTI). For FY2021, no LTI award was made. The status, amount and metric that formed the basis for prior LTI awards is also disclosed. We note that awards are made in Chorus shares (rather than options) with the company retaining an ability to 're-test' LTI awards for 12 months post vesting; both policies are supported by NZSA. We note that a shareholding requirement has been introduced for executives receiving an LTI award.

We note that the maximum opportunity for CEO STI exceeds base salary, a position not generally supported by NZSA. The level of variable remuneration is also weighted towards STI, rather than LTI; NZSA prefers to see a greater weighting towards long-term shareholder return.

NZSA also appreciates disclosure of the notice periods associated with the CEO's contract, although there is no disclosure as to whether any additional termination benefits are payable.

Board Composition: Generally good disclosure. The company discloses a 'collective' skills matrix outlining how the Board matches the skills required to govern the company, although an 'individual' matrix is not disclosed. We note that the company does not participate in the IoD's "Future Directors Programme"; given the scale and status of Chorus, NZSA feels that participation would support the development of emerging directors within New Zealand.

Director Tenure: NZSA looks for evidence of ongoing succession or ‘staggered’ appointment dates that allow effective knowledge transfer in the event of succession. We note the company has a range of appointment dates, providing evidence of succession planning and ensuring that the company can manage director succession effectively (thereby reducing the risk of knowledge loss for investors).

We note that one director, Prue Flacks, has served on the Board for more than 9 years, a general benchmark for succession planning. The company noted that Prue’s resignation was signalled at last year’s Annual Shareholder Meeting. NZSA appreciates this clear signal in relation to succession, in order to ensure long-term governance sustainability.

ASM Format: While NZSA prefers ‘hybrid’ ASM’s (ie, physical and virtual) as a way of promoting shareholder engagement while maximising participation, we understand the company’s approach in planning a virtual-only meeting given the current Covid-19 restrictions across New Zealand.

Audit

NZSA assessment against its key policy criteria is summarised below:

Policy Theme	Assessment	Notes
Audit independence	G	Good disclosure
Audit rotation	A	See comment below.

Audit Rotation: Whilst the company ensures the Lead Audit Partner is rotated at 5 years it does not disclose whether the Audit Firm is rotated at 10 years. In common with many other NZX-listed companies, it also does not disclose the appointment date of the Audit Firm or the Lead Audit Partner.

Ethical and Social

NZSA assessment against its key policy criteria is summarised below:

Policy Theme	Assessment	Notes
Whistleblowing	G	Good disclosure
Political donations	G	Disclosed – no political donations

Financial & Performance

Policy Theme	Assessment	Notes
Dividends and Imputation	A	See comment below.
Capital Raise process	n/a	There was no capital raising

Dividend: We note the dividend was 25 cents share whilst the earnings per share was 11 cents.

Prior investor presentations have given a thorough rationale of dividend policy, including changes as the company's activities gradually move from 'build' to 'operate' in relation to its network. The company's dividend policy is based on operating cashflows less required 'sustaining' capex (free cash flow), although there is a transition period to reflect existing capex and funding (credit) requirements

Metrics Overview:

Chorus's share price fell from \$8.51 to \$6.54 (as of September 27th) over the last 12 months – a 23% decline. This compares unfavourably with the NZX 50 which increased by 13% in the same period. The Performance Factor for CNU is -1.79.

Metric	2021	2020	Change
Revenue	\$947m	\$959m	-1%
EBITDA	\$649m	\$648m	n/c
NPAT	\$47m	\$52m	-10%
EPS ¹	\$0.105	\$0.117	-10%
PE Ratio	62	73	
Current Ratio	0.44	0.22	99%
Debt Equity	5.18	5.09	2%
Operating CF	\$556m	\$474m	17%
Cash flow (cps)	\$1.24	\$1.07	17%
NTA Per Share ¹	\$1.75	\$1.73	2%
Dividend Per Share ¹	\$0.25	\$0.24	4%

¹ per share figures based off actual shares at balance date (not weighted average)

2020 was a mixed year for Chorus with revenues falling slightly, NPAT falling by 10%, but an increased fully imputed dividend of \$0.25 paid to shareholders.

Operating cashflows were up by 17% to \$556m and these are the driver for the valuation of Chorus. Measured in cent per share, operating cashflows were \$1.24. To be more precise, it is the expectation of future operating cashflows that drive valuation.

NTA per share is \$1.75 and CNU trade at a large premium to their NTA.

Of note, it is interesting to see that the per-share free cash flow (which includes sustaining capex) exceeds EPS. This, perhaps, implies that future asset renewal will be less expensive than the original asset.

CNU have relatively high debt levels with their debt equity ratio at 5.18. Two items called Crown Funding and Crown Infrastructure Partners Securities comprise \$1,473m of non-current liabilities. In addition, interest bearing debt increased by \$341m to \$2,233m. Total non-current liabilities are \$4,451m. This is large when compared to total equity of \$948m.

CNU provided guidance for FY22, when announcing their FY21 results. This guidance is subject to no material changes in regulatory or competitive outlook. Guidance is similar to FY21.

- EBITDA: \$640-\$660 million

- Capital Expenditure: \$550-\$590 million
- FY22 initial dividend guidance of 26 cents per share

Resolutions

1. To re-elect Patrick Strange as an Independent Director.

Patrick Strange was appointed to the Board in April 2015 and is the Chair. He is currently Chair of Auckland International Airport, and a Director of Mercury. He was formerly Chief Executive of Transpower.

We will vote undirected proxies **IN FAVOUR** of this resolution.

2. To re-elect Murray Jordan as an Independent Director.

Murray Jordan was appointed to the Board in September 2015. He is a Director of Metlifecare, Metcash Limited (an ASX listed company), Southern Cross Medical Care Society, Southern Cross Healthcare Limited, SkyCity and Stevenson Group, and a Board trustee of Starship Foundation.

We will vote undirected proxies **IN FAVOUR** of this resolution.

3. To elect Miriam Dean as an Independent Director.

Miriam Dean is a Queen's Counsel with more than 38 years' experience in commercial dispute resolution and 25 years' experience in governance, with a specialty in competition, consumer, and regulatory law. She is a Director of Ōtākaro Limited (the Crown-owned company responsible for the central city anchor projects following the Canterbury earthquake). She is also Chair of the Banking Ombudsman Scheme, Deputy Chair of the Real Estate Institute of New Zealand, and a member of a number of central and local government-related advisory boards. In addition, she is regularly asked to carry out government and nongovernment inquiries and reviews.

We will vote undirected proxies **IN FAVOUR** of this resolution.

4. That the Board is authorised to fix the auditor's remuneration for the coming year.

This is an administrative resolution.

We will vote undirected proxies **IN FAVOUR** of this resolution.

You can vote online or appoint a proxy at <https://www.investorvote.com.au/>

Instructions are on the Proxy/voting paper sent to you.

Voting and proxy appointments close **12.00pm Monday 25 October 2021.**

Please note you can appoint the Association as your proxy. We will have a representative attending the meeting.

STANDING PROXIES - AUTOMATICALLY APPOINT NZSA AS YOUR PROXY

MAKE YOUR VOTE COUNT!

Details on the NZSA website.

<http://www.nzshareholders.co.nz/shareholders-standing-proxies.cfm>

The Team at NZSA