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Blackmores changing of the guard

Company/ASX Code	Blackmores/BKL
AGM date	Tuesday 27 October 2020
Time and location	11am Lumiagm.com/351863503
Registry	Computershare
Webcast	Yes
Poll or show of hands	Poll on all items
Monitor	Julieanne Mills and Carol Limmer
Pre AGM Meeting?	Yes, with Chairman: Brent Wallace, Christine Holman: Chair, People and Remuneration committee, Alastair Symington: CEO, Gunther Burghardt: CFO, and Cecile Cooper: Company Secretary

The individuals (or their associates) involved in the preparation of this voting intention have a shareholding in this company.

Item 1	**Consideration of accounts and reports**
ASA Vote	No vote required

Summary of ASA Position

Another very disappointing year for Blackmores which has just commenced a three year transformation process under the new CEO Alastair Symington, and has to contend with the impact from COVID, the subsequent impact to supply chain, drop in Chinese tourist and student sales, and regulatory changes in China. Net sales of $568m were down 3% and profit dropped 66% to $18.1m. No interim or final dividend will be paid for the 2020 financial year (FY20).

The Braeside manufacturing plant, purchased from Catalent in 2018 and completed in October 2019, has transformed Blackmores into a vertically integrated company that can now manufacture its own products. This will provide many advantages including better product control, more responsive production time and flexibility, and eventually drive down cost of goods. Registration of goods is also much simpler with a manufacturing plant. The ability to produce halal certification and vegan products provides growth areas here and internationally.

However, it hasn't been without its problems. Integrating Braeside into the company will take three years and there is more pain to come. Costs of this integration have impacted the profit for FY20 with a $17m increase in cost of goods (COGS).

The sectors that did well this year were, Blackmores International (excluding China) which continued to grow with revenue of $139m and up by 30% compared to the prior year. BioCeuticals also continued to perform strongly with revenue of $99m and a 7% increase year on year, due largely to the demand for its Armaforce product during COVID.

Australia and China however were the big underperformers. Australia's revenue was $227m down 14.8%, driven largely by the decline in Chinese shoppers and slowdown in products other than immunity during COVID. China's revenue was $103m down 16% but its profit (EBIT) was reported as negligible at $244,000 down 98% from 2019.

The company had early warning of COVID in February with the impact in China felt across supply chains and freight issues. In March weekly director meetings and business continuity management groups were set up to ensure a safe working environment for employees, and office staff were supported to work from home. There was a 20% reduction of pay and hours for all employees including KMP and the board (with some exclusions for staff needed for continued supply) agreed. It was initially to cover 4 months to the end of the FY however this was able to be reduced to 6 weeks due to introduction of JobKeeper.

The company received around $1m in JobKeeper for its BioCeuticals sector and Singapore Job Support Scheme payments for Singapore staff. BKL also received $2m in Jobkeeper June payments in July 20. However, the addition of foreign issued shares with the capital raise, has created a "GST free supply" and triggered a change to revenue that may mean BKL is ineligible for $1.4m of payments. Until resolved this amount has been excluded from pre-tax income and excluded from underlying profit but not NPAT.

Blackmores was deemed an essential service during COVID and has been able to stay open through the lockdowns, including the latest Victorian lockdown.

The CEO's new global strategy sees the development of an Innovation Centre in Shanghai to garner consumer insight into what the modern Chinese career woman wants. BKL have just launched a new premium X range of high end products around modern parenting, and to capitalise on the Australian reputation for quality products. It has grown its market share of cross border e-commerce in the Chinese vitamins and dietary supplements market to 5%. There is a lot of competition in this VDS sector but BKL sees a future in the premium market.

Governance and culture

There is an urgent need for board replacements (as discussed below) along with independence and gender balance in line with their aspirations of 50% women on the board by 2025. The KMP is currently only 20%. Women are well represented elsewhere with 55% at executive level, and 70% women within the broader workforce. BKL has 99% pay equity, their employee engagement is high and they are recognised as an generous and considerate employer. 91% felt safe and connected during COVID

The introduction of a new minimum shareholding policy is to be commended. Commencing from June this year NEDs will be required to hold shares to the value of one year's base fees (not inclusive of committee fees) within 3 years, based on the share price at the time of purchase. From August 20 the CEO is now required to have the equivalent of 100% of FAR within 5 years and other KMP 50% of FAR within 5 years.

In line with BKL overall sustainability goals the CEO announced a new commitment to net zero emissions by 2030. We look forward to plans on how to achieve and measure this in the next sustainability report. Sustainability is a specific non-financial target in the incentive remuneration.

There has been separation of board Audit and Risk into two committees. The committees currently have the same directors and there are no additional fees. When more directors are on board this will provide an opportunity for different skill sets to be applied with different directors, also it allows for more time and focus on risk and risk management.

Concerns around a potential change in culture, with all the changes to management, were discussed at the pre-AGM meeting, and we were assured that the new personnel, have a clear understanding and are aligned with the existing purpose and values of BKL.

A new Speak up program provides anonymous reporting of unethical or inappropriate behaviour in the work force or across the supply chain.

BKL group contributes to the community in many areas and this year was no exception with the $85,000 to the Red Cross for bushfires, along with matched contributions from Marcus Blackmore. BKL product care packages were sent to front line and emergency workers here and overseas during COVID.

Financial performance

A $50m efficiency program was announced in Feb. This will see 10% of the 1400 workforce, mainly in sales and marketing lose their jobs in the coming months.

No dividend was declared for FY20.

Another price increase that has just been implemented will hopefully add to the bottom line.

Key events

The Catalent -Braeside manufacturing purchase was completed in October 2019.

Streamlining of brands and product ranges continues with the post June 30 sale of Wheyless and Isowhey for $1.09m in August 20. BKL have also placed Global Therapeutics up for sale.

The sale of excess land at Warriewood for $5.2m is expected to be complete in Feb 2021.

In May 2020 BKL announced a successful $92m Institutional placement at $72.50, representing 7.3% of shares on issue. This was followed by a $25m SPP at $72.50. With a total of $77m of applications for the SPP it was scaled up due to shareholder demand to $49m. The scale back was based on a minimum issuance of $1000 and the legal cap of $30,000 and the allocation was on a pro-rata basis to holdings, rather than demand.

The $141m capital raising will be used for cash reserves, to invest in growth markets in India, Indonesia and China and to fast track digital transformation.

Gearing is now down from 31% to 11%, with $34m less debt since the fundraising.

Key board or senior management changes

FY20 saw significant change across the board, KMP and executive team. The resignation of Directors, Jackie McArthur and Helen Nash on the 5 August 2019 was soon followed by the appointment on the 16 September 2019 of Alistair Symington as CEO and managing director. In 2019 the chairman, Brent Wallace announced his plans to retire as soon as a new chairman is found. John Armstrong announced his immediate resignation in September 2020.

Currently Christine Holman, Brent Wallace and David Ansell, are the remaining independent directors, along with executive director Marcus Blackmore and CEO/MD Alastair Symington. Given COVID and the extra workload that has added to a director’s responsibilities, we look forward to the announcement of further directors and a new chair.

David Ansell has become the interim chair of Audit and Risk committees since John Armstrong's resignation. Director Christine Holman became the new chair of the People and Remuneration Committee.

There is a plan to reduce the board from its original eight directors down to seven. Once a new chairman has been announced Marcus Blackmore, will step down as an executive director to become a non-executive director, and his fees will be reduced accordingly. The new chair and another two independent directors will provide more independence. We hope to have an announcement by the AGM.

Alastair Symington's new growth and transformation strategy saw significant change at executive level and a new executive structure (see below in Remuneration). The CFO, Aaron Canning was replaced by Gunther Burghardt in January 2020. The managing director of Asia, Peter Osborne was replaced by his deputy Dean Garvey who became managing director of International (excluding China) in December 2019. China became a separate sector and Kitty Lui was appointed managing director in December 19. Ayumi Uyeda was appointed to the role of managing director of Australia & New Zealand in June 2019. Joanne Smith was appointed to the new role of chief Marketing and Innovation in March 20.

ASA focus issue

It was disappointing that the capital raising didn't use a PAITREO system however the outcome was not necessarily unfair for most shareholders. (See Key Events above)

Financial Summary

(As at FYE)	**2020**	**2019**	**2018**	**2017**	**2016**
NPAT ($m)	18.1	53	70	59	100
UPAT ($m)	18.7	55	N/A	N/A	N/A
Share price ($) at 30 June 20	77.95	89.91	142.5	95.84	131.39
Dividend (cents)	0	220	305	270	410
TSR (%)	-13%	-35%	52%	-25%	80%
EPS (cents)	103.5	309.2	406.4	342.6	580.6
CEO total remuneration, actual ($m)	1.347	0.79	2.09	4.32	1.95

For 2020 the CEO's total actual remuneration was **15 times** the Australian Full time Adult Average Weekly Total Earnings (based on May 2020 data from the Australian Bureau of Statistics).

Item 1	Adoption of Remuneration Report
ASA Vote	**For**

Summary of ASA Position

2020 Remuneration Plan

CEO rem. framework	Target* $m	% of Total	Max. Opportunity $m	% of Total
Fixed Remuneration	1.3	38%	1.3	24%
STI - Cash	.390	12%	.780	14%
STI - Equity	.390	12%	.780	14%
LTI	1.3	38%	2.6	48%
Total	3.38	100.0%	5.46	100%

The amounts in the table above are the statutory amounts that are envisaged in the design of the remuneration plan. *Target remuneration is sometimes called budgeted remuneration and is what the company expects to award the CEO in an ordinary year, with deferred amounts subject to hurdles in subsequent years before vesting.

FY20 has seen considerable change to the KMP and executive team as mentioned above. The appointment of CEO Alastair Symington was a significant investment that the company felt it needed to make to transform Blackmore into a world class organisation, rejuvenate the brand and deliver new growth. According to the board his remuneration along with the other new personnel has been benchmarked against peers to attract the best talent. It appears on the generous side compared to comparative $1.2bn market cap companies.

Changes have been made to the executive structure. Key management personnel (KMP) now includes only the CEO, CFO and executive and non-executive board directors. Direct reports to the CEO, the executive team (ET), have also been included in the remuneration report to make comparisons with last year a little clearer. It is difficult to compare the past costs to the current costs especially with Marcus Blackmores lower CEO FAR in 2019, redundancies and partial year fees. Overall, however it does look to be significantly more, the combined remuneration for KMP and the executive team for 2020 was $6.85m whereas in 2019 it was $5.43m.

The remuneration report is very detailed and transparent with actual and statutory remuneration included.

The CEO’s remuneration is broken into fixed annual remuneration (FAR), short term incentives (STI) long term incentives (LTI), profit share scheme (PSS), and staff share plan (SSP).

Fixed remuneration has remained the same across KMP and the ET with the exception of the COO whose FAR was increased to take into account the increased responsibilities with the new Braeside manufacturing and supply streams.

The STI is determined based on corporate and individual targets. A Group NPAT threshold gateway applies as well as appropriate standards relating to brand, reputation, safety and quality. After a threshold amount of $50,000, 50% is paid in cash and 50% deferred into performance rights that vest after one year and continuous employment.

No STI was paid to CEO and KMP for FY20 because the gateway NPAT performance hurdle of $53.4m had not been met.

The LTI performance rights are based on meeting specific targets of equally weighted EPS growth and ROIC over a three year period. The ASA would like to see the LTI over a longer time frame of at least four years. There is a 5% threshold for three year compound annual growth rate (CAGR) in EPS. The number of performance rights will be calculated using the VWAP 14 days before and after the financial results in August. No dividends are paid on unvested shares.

The maximum LTI opportunity has been increased from 150% of FAR to 200% of FAR in 2020. The ASA has concerns around the quantum of his total potential remuneration package given the size of the company. Concerns also that the current NPAT is so low and that going forward the LTI targets will not necessarily be difficult to achieve.

No LTI for the FY 2018 Plan was awarded because the three-year EPS growth target was not met.

The Profit Share Scheme (PSS) is available to all eligible employees, it is a pro-rata distribution based on up to 10% group NPAT. Blackmores profit share of $1.5m was paid out to all eligible employees in the 1H, no 2H payment was made. This year's distribution was the equivalent to 4 day's pay. Mr Symington's distribution for FY20 was $9687.

The Staff Share Plan (SSP) All employees are eligible to contribute $1000-$10,000 of their salary to purchase company shares. At the end of the year the company would usually provide 1 free share for every 3 shares purchased by an employee in that financial year. This is capped at $500,000. In 2020 it was determined that **no share matching** would occur.

Clawback can be applied at discretion of the board.

There was an independent review of the STI and LTI framework in 2020 and Blackmores has made positive changes to its remuneration framework.

The **2021 remuneration plan**

There will be no increase in FAR to CEO and ET in 2021.

STI reward framework

The $50,000 cash threshold payment has been removed and the STI is now split 50/50 cash and equity. The equity is now deferred for two years for the CEO and vests at the end of this period.

A gateway threshold of 90% EBIT must be met prior to the plan activating. Performance measures include: group financial 70%, group strategic 20%, and group non-financial 10% and are described in the annual report on page 51. The deferred STI equity value will be determined using VWAP.

The LTI framework is much the same as 2020.

Ned fees remained the same having been increased in 2019, however the chairman's fee will be increased in 2021 from $254,000 to $305,000 upon appointment of the new chairman. These fees have also been benchmarked against peers by the board. They are at the top end of the range for a company with market cap of $1.2bn however that may be what is required to attract a new chair.

Overall the remuneration plan does seem generous, however, there are clear goal posts and financial gateways, there is a significant proportion at risk and there is also the possibility of clawback. Given the poor financial performance there has been no STI and LTI awarded, no share matching of the staff share plan and no 2H distribution of profit share for FY20.

Item 2	Re-election of David Ansell as a Director
ASA Vote	For

Summary of ASA Position

David Ansell was appointed to the board in October 2013.

His professional career includes sales and marketing in the beverage industry, CEO of advertising agency Saatchi and Saatchi in (1999-2002) and managing director of Mars Inc Australia (2002-2012). He has a firm belief and understanding of brand and consumer, a strategic skill set and has led companies through difficult turn arounds.

He is currently managing director and chair of Jacobs Douwe Egberts (ANZ) and a director of Cycling Australia.

He is a member of the People and Remuneration Committee, the and interim chair of Audit Committee and the Risk Committee.

His shareholding of 1,413 shares is equivalent to $110k (at a 30 June share price) The ASA likes to see directors with more "skin in the game". David has been a director for seven years and does not have the equivalent of one year's base fees of $146,000.

The ASA have some concern around David's managing director and chair role at Jacobs Douwe and the time commitments that that role entails, especially with the current COVID demands. The ASA also has concerns with the number of women on the board. Given the opportunity to fill other spots with women, the vacant positions, and recent loss of directors we will support his re-election to maintain stability.

Item 3	Approval of STI grant to CEO/Managing Director Alastair Symington under the ESP.
ASA Vote	For

Summary of ASA Position

In FY21 the executive plan has been altered to remove the $50,000 cash threshold. The STI will now be paid 50% in cash and 50% in deferred equity (two years). This change is welcomed as it provides further shareholder alignment. The main measure is NPAT growth and non-financial targets as set by the board along with continued employment.

The maximum number of share rights that could be granted under the STI is determined by dividing $780,000 (60% FAR) by the VWAP (14 days before and after the financial results in August 2021).

Item 4	**Approval of LTI grant to CEO/Managing Director Alastair Symington of up to 38,364 shares under the ESP.**
ASA Vote	**For**

Executive Share Plan will be awarded based 50/50 on EPS CAGR (Earnings per share compound average growth rate) & ROIC (return on invested capital) with a minimum set by the board as set out in the annual report on pg 51. The maximum that could be granted to Mr Symington under the LTI is 38,364 performance rights is based on 200% of his FAR (150% of FAR in FY19).The FY20 shares have been valued at $67.77 based on the VWAP (14 days before and after the financial results in Aug 2020).

The ASA would prefer that shares are purchased on market but given the uncertain economic climate it is understandable that the board want the flexibility to decide at vesting.