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Tough times for the new CEO

Company/ASX Code	GUD Holdings/GUD
AGM date	Thursday 24 October 2019
Time and location	10am RACV Club Level 17 501 Bourke Street Melbourne
Registry	Computershare
Webcast	No live webcast, recording available on their website within two days
Poll or show of hands	Poll on all items
Monitor	John Whittington assisted by Christine Haydon
Pre AGM Meeting?	Yes, with Chair Mark Smith, Chair of Remuneration Committee David Robinson, and Company Secretary Malcolm Tyler

Item 1	**Financial Statement and Reports**
ASA Vote	No vote required

Summary of ASA Position

<u>Financial performance</u>

GUD can now be described as a strongly performing automotive aftermarkets distributor (accounting for 76% of revenue and over 100% of profit) with one other division, Davey (pumps), which may be divested in the near future.

In the 2019 financial year (FY19), whilst total group revenue was flat at $434m, revenue from continuing operations (excluding the divested Oates business) increased by 9%. Automotive revenue was up 12% and revenue at Davey was up 3%.

Reported net profit after tax (NPAT) for the year was $59.6m, down 42% from last year's reported result which included the gain on sale of Oates, but up 18% on a continuing basis. Automotive NPAT was up 3% and Davey NPAT was up 222% from a very low base.

Cash flow from operations was down 25% (to $44.5m) and free cash flow (excluding the proceeds of the sale of Oates) was down 53%.

Dividends increased 8% to 56 cents per share however total shareholder return (TSR) for the year was -26% (-29.3% from the decrease in the share price and +3.7% from dividends).

The market didn't seem to like the results with the share price declining from $10.10 to $9.67 on the day of the results and dropping as low as $8.43 a few weeks later.

<u>Key events</u>

Disc Brakes Australia was acquired in July 2018.

Key Board or senior management changes

Jonathan Ling who had been CEO since 2013 retired on 30 September 2018 and was replaced by Graeme Whickman, formerly President and CEO of Ford Australia and New Zealand. Guy Nicholls, the CEO of Ryco, GUD's largest single business unit, left GUD to join a customer in May 2019.

ASA focus issue

Board skills seem appropriate and are fairly well disclosed. Diversity is poor and we believe one of the directors is significantly overloaded.

Remuneration disclosure is generally satisfactory, long-term incentive awards are based on face value, and the table of actual remuneration has been improved this year.

"Skin the game" is not ideal with director and executive equity holdings (other than the Chair) less than we would like. We are calling on GUD to implement a shareholding policy.

Shareholder participation during the year has been satisfactory.

Summary

(As at FYE)	2019	2018	2017	2016	2015
NPAT ($m)	59.6	101.8	(7.3)	(43.0)	33.2
UPAT ($m)	59.6	50.5	51.5	(40.9)	31.1
Share price ($)	10.01	14.16	12.91	9.11	8.84
Dividend (cents)	56	52	46	43	42
TSR (%)	(26)	13	46	8	49
EPS (cents)	68.9	58.6	60.1	(48.0)	43.0
CEO total remuneration, actual ($m)	1.275*	2.456	2.578	1.666	1.174 (part year)

* This represents the combined pay of the previous CEO who received $0.524m actual remuneration for the period 1 July to 30 September 2018 and the new CEO who received $0.750m for the period 1 October 2018 to 30 June 2019.

For FY19, the CEOs' total actual remuneration was **14 times** the Australian Full time Adult Average Weekly Total Earnings (based on May 2019 data from the Australian Bureau of Statistics).

Item 2.1	**Re-election of Mark Smith**
ASA Vote	**For**

Summary of ASA Position

Mr Smith, a former Managing Director and executive at Cadbury Schweppes, Unilever, and Uncle Toby's, was appointed to the board in May 2009. He has a shareholding equivalent to 186% of his total remuneration (as at year end) and is independent.

He is currently Chair of one other listed company (Australian Pharmaceutical Industries). We do not consider this workload excessive.

We believe that Mr Smith is well qualified to contribute to the board, has sufficient “skin in the game”, and we support his re-election.

Item 2.2	**Re-election of Graeme Billings**
ASA Vote	**Against**

Summary of ASA Position

Mr Billings, an auditor and former senior partner of PricewaterhouseCoopers, was appointed to the board in December 2011. After eight years on the board he has a shareholding equivalent to 74% of his total remuneration (as at year end) and is independent.

Mr Billings is chair of two listed companies (Korvest and Azure Healthcare) and a non-executive director of three others (GUD, Clover Corporation, DomaCom) as well as Chair of two unlisted companies (Matthews Steer and ANCA). We consider this workload excessive.

We believe that Mr Billings is highly regarded by fellow board members and is well qualified to contribute to the board. His attendance at Board and other Board committee meetings is impeccable.

We are, however, concerned that his high workload will not allow any room for further unexpected events amongst his company responsibilities. We therefore cannot support his re-election although If he were to indicate a reduction in workload during his presentation at the AGM or responding to our questioning at the AGM, we will review our voting decision.

Item 3	**Remuneration Report**
ASA Vote	**Against**

Summary of ASA Position

CEO remuneration framework

	Target $m	% of Total	Max. Opportunity $m	% of Total
Fixed Remuneration	0.750	64%	0.750	50%
STI - Cash	0.196	17%	0.295	20%
STI - Equity	-	0%	-	0%
LTI	0.221	19%	0.443	30%
Total	1.167	100%	1.488	100%

The remuneration structure is essentially unchanged from the past three years. It has three components – fixed remuneration, short term incentives (STI) and long-term incentives (LTI).

The STI provides an annual cash value bonus for achieving or exceeding and agreed cash value added (CVA) target. The CVA target for each business unit and the Group overall is established during the budget process prior to the commencement of the financial year.

LTI is based on the Group's total shareholder return (TSR) relative to a comparator group (ASX Small Ordinaries index) and is provided as performance rights which can be converted to shares if the performance hurdle is achieved. The LTI award has an additional hurdle that the absolute TSR must be positive.

We believe that disclosure is good and certain aspects of the policy are satisfactory. We like CVA as a target for STI bonuses and that they are only be paid where CVA performance exceeds the CVA performance of the prior year and the CVA target of the relevant business unit. However, we are still disappointed with the following areas:

- STI awards are paid entirely in cash
- LTI awards have no holding lock, are based only over three years, and are based on relative TSR based on a generic (ASX Small Ordinaries) index rather than comparable companies or groups

The layout of the report is also little changed from last year although there have been minor changes to the table of actual remuneration which we believe makes it more understandable. As a result of a new CEO being appointed, the level of CEO pay has also been significantly reduced.

Last year we supported the report this year with the following wording "In recent years we have opposed the report whilst acknowledging it is close to the line. Given the addition of an absolute TSR hurdle to the LTI we want to acknowledge this improvement and will support the report this year. We do note however that the report is still very close to the line and we would expect further improvements before we could support it again in the future."

Given there has been little substantive improvement this year we will not support the remuneration report but acknowledge that it is close to the line and some more substantive improvements next year would enable us to support it then.

Item 4	**Approval of LTI grant to Managing Director Graeme Whickman**
ASA Vote	**For**

Summary of ASA Position

This is for the issue of a maximum of 58,686 performance rights worth $596,400. This is equivalent to 60% of fixed remuneration.

The shares will vest based on the relative shareholder return of the company compared with the ASX small ordinaries index (excluding mining, materials, and resource industries) over the period 1 July 2018 to 30 June 2022. If the company TSR over this period falls below the 50th percentile of the comparator group, no shares will vest. If the TSR falls between the 50th and 75th percentile then a linear scale will apply from 50% vesting at the 50th percentile up to 100% vesting at the 75th percentile. If the TSR exceeds the 75th percentile then 100% of the shares will vest. ***In addition***, the Company's absolute TSR must be positive over the performance period for any Performance Rights to vest.

All rights will lapse if Mr Whickman's employment is terminated for cause and clawback of this award may occur in cases of fraud or misconduct. In the case of resignation, retirement, redundancy, or termination by the Company for convenience, a pro-rata number of rights will be retained and will vest only if the above performance hurdles are met.

This award is not ideal in that it is based on only one hurdle and has a vesting schedule which we find too steep (we would prefer 30% vesting at the 50th percentile scaling to 100% vesting at the 85th percentile) and is over too short a period (we would prefer four or five years). On the other hand, we believe the maximum award is not excessive, the calculation of the award is based on face/market value, it is quite transparent (more so than last year), relatively easy to understand, and is in appropriate proportion to fixed remuneration.

We believe this is a line-ball decision. Our intention is to support this resolution but with a similar proviso to the remuneration report, ie that we expect to see further improvement next year before we would support it next year.

The individual (or their associates) involved in the preparation of this voting intention has no shareholding in this company.