



Financial results down-hill but better future foreshadowed again

| | |
|------------------------------|--|
| Company/ASX Code | Hills Limited/HIL |
| AGM date | Friday 8 November 2019 |
| Time and location | 2:30pm Adelaide Convention Centre |
| Registry | Link Market Services |
| Webcast | No |
| Poll or show of hands | Show of hands |
| Monitor | Bob Ritchie assisted by Malcolm Keynes |
| Pre AGM Meeting? | No, due to ASA unavailability |

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

Summary of ASA Position

Governance and culture

First the good news: Board fees have been reduced significantly to conform to other companies of similar size.

Financial performance

Unfortunately, for the 2019 financial year (FY19) there was also a large negative turn-around in operating cash flow, and another significant impairment. There was no dividend for fourth consecutive year and shareholder returns negative for the fourth time in the last five years. With accumulated loss now at 73.7 cents per share over the last five years. Market capitalisation has to shrunk to \$46 million; 0.88 times book value of \$52 million.

Key Board or senior management changes

A non-executive director (NED) Mr Alan Kincade, joined the board and resigned after a few months.

Summary

| (As at FYE) | 2019 | 2018 | 2017 | 2016 | 2015 |
|--------------------------------------|--------|-------|--------|--------|---------|
| NPAT (\$m) | -8.8 | 0.4 | -7.9 | -68.31 | - 85.95 |
| UPAT (\$m) | 0.5 | 0.04* | -11 | -0.78 | -11.1 |
| Share price (\$) | 0.175 | 0.23 | 15.5 | 24.5 | 0.23 |
| Dividend (cents) | 0 | 0 | 0 | 0 | 2.1 |
| TSR (%) | -23.9% | 48.4% | -36.7% | -46.2% | -72.6% |
| EPS (cents) | -4.1 | 0.2 | -3.4 | -29.4 | -37.0 |
| CEO total remuneration, actual (\$m) | 0.42 | 0.39 | 0.38 | 0.90 | 0.89 |

*estimated

For FY19, the CEO's total actual remuneration was **4.7 times** the Australian Full time Adult Average Weekly Total *Earnings* (based on May 2019 data from the Australian Bureau of Statistics).

Note - For May 2019, the Full-time adult average weekly total earnings (annualised) was \$88,145 (<http://www.abs.gov.au/ausstats/abs@.nsf/mf/6302.0>, "Full-time adult average weekly total earnings", Trend(a)).

| | |
|-----------------|--|
| Item 2 | Re-election of Ms Fiona Bennett as a Director |
| ASA Vote | Against |

Summary of ASA Position

Ms Bennett is well qualified and has been a director for nine years. She was a director when the company name was changed from Hills Industries to Hills Consolidated, reflecting a strategy which embraced the 'legacy industries' relating to steel. And a couple of years later when the name changed to Hills, reflecting departure from the legacy industries. And when over \$200 million of cash raised by sale of assets was used to buy businesses which were subsequently impaired at a discount of about 75%. And more recently when distribution centre assets were acquired and in FY19 were impaired by \$6 million (AR p55). While we acknowledge a board make decisions as a group, the outcomes have been poor and there is no sign of outcomes improving which suggests to us the directors need to change.

Our present intention is to vote against re-election but we will ask questions, searching for information which disqualifies the foregoing analysis.

| | |
|-----------------|--|
| Item 3 | Re-election of Mr Ken Dwyer as a Director |
| ASA Vote | Undecided |

Summary of ASA Position

Mr Dwyer has been a director for three years. It is unclear whether the company acquired recently impaired assets of the distribution centre before or after he joined the board. The annual report does not give better identification of the impaired assets beyond, 'distribution centre asset' and 'intangible assets' (AR p55). This makes it difficult to be better informed. We will ask. If Mr Dwyer was party to the impaired asset acquisition, we will seek reconciliation between his prior experience and expertise with finance and a distribution centre and his present activity in investment and venture capital on the one hand and what seems at least in hindsight to be a poor capital decision by the board.

| | |
|-----------------|--|
| Item 4 | Adoption of Remuneration Report |
| ASA Vote | For |

Summary of ASA Position

Managing director remuneration scheme includes an short-term incentive (STI) of 75% of fixed remuneration and no long-term incentive (LTI), contrary to ASA guidelines. Half STI achieved is in cash and the other half is paid in shares over three years: 20% in the first year, 30% the next year and 50% a year later. This scheme does not conform to ASA guidelines insofar as it provides no performance test beyond one year and incentive is less than fixed income. It conforms in providing half STI payment in equity. The total package, however, is reasonable in quantum, structured for the company's circumstance, and a 'fair value' fiddle is not used to expand the number of shares.

| CEO rem. framework | Target \$m | % of Total | Max. Opportunity \$m | % of Total |
|--------------------|------------|------------|----------------------|------------|
| Fixed Remuneration | 0.35 | 58% | 0.35 | 58% |
| STI - Cash | 0.125 | 21% | 0.125 | 21% |
| STI - Equity | 0.125 | 21% | 0.125 | 21% |
| LTI | 0 | 0% | 0 | 0% |
| Total | 0.6 | 100.0% | 0.6 | 100.0% |

The amounts in the table above are the statutory amounts that are envisaged in the design of the remuneration plan.

In FY19 the second of two tranches, each of 100,000 shares (worth less than \$20,000) vested upon passage of time in employment; a sign-on remuneration – also a feature opposed in ASA guidelines.

In FY19 none of the 70% of STI was awarded for financial performance and half the 30% non-financial component of STI was awarded. For FY20 the financial component has been increased to 80% of STI and the non-financial component of 20% has been reduced in scope to only employee engagement.

Board fees were reduced significantly in FY19, bringing them more into line with other companies of Hills' market capitalisation.

For a company which has a book value of only \$52 million and a market capitalisation of \$46 million and is struggling with significant challenges, the remuneration arrangements are understandable as they match the company's circumstances.

While Hills' remuneration report still contains significant elements of non-compliance with ASA guidelines, there have been significant improvements in policy this year and practice has demonstrated good judgement. In resolving to support this resolution, we are placing strong reliance on last year's advice from the chairman of remuneration committee, that the current arrangements designed for challenging circumstances should not continue beyond what is now another two or three years.

| | |
|-----------------|--|
| Item 5 | Renewal of proportional takeover provisions |
| ASA Vote | For |

Summary of ASA Position

These proposals are normally non-controversial where a company renews its constitutional provisions which don't allow a predator to only bid for a proportion of a shareholders' interest. We prefer full takeovers so that shareholders are not left with a controlling shareholder and would usually support these resolutions.

ASA supports this resolution..

The individual(s) (or their associates) involved in the preparation of this voting intention have shares in this company.

ASA Disclaimer

This document has been prepared by the Australian Shareholders Association Limited ABN 40 000 625 669 ("ASA"). It is not a disclosure document, it does not constitute investment or legal advice and it does not take into account any person's particular investment objectives. The statements and information contained in this document are not intended to represent recommendations of a particular course of action to any particular person. Readers should obtain their own independent investment and legal advice in relation to the matters contemplated by this document. To the fullest extent permitted by law, neither ASA nor any of its officers, directors, employees, contractors, agents or related bodies corporate:

- *makes any representations, warranties or guarantees (express or implied) as to the accuracy, reliability, completeness or fitness for purpose of any statements or information contained in this document; or*
- *shall have any liability (whether in contract, by reason of negligence or negligent misstatement or otherwise) for any statements or information contained in, or omissions from this document; nor for any person's acts or omissions undertaken or made in reliance of any such statements, information or omissions.*

This document may contain forward looking statements. Such statements are predictions only and are subject to uncertainties. Given these uncertainties, readers are cautioned not to place reliance on any such statements. Any such statements speak only to the date of issue of this document and ASA disclaims any obligation to disseminate any updates or revisions to any such statements to reflect changed expectations or circumstances.