Australian Shareholders' Association

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Jumbo's jumbo sized margins squeezed by rising costs.

Company/ASX Code	Jumbo Interactive Ltd / JIN
AGM date	Thursday, 10 November 2022
Time and location	11:00 am Brisbane time Jumbo offices, Level 1, 601 Coronation Drive, Toowong, 4066
Registry	Computershare
Type of meeting	Hybrid
Poll or show of hands	Poll on all items
Monitor	Paul Donohue and Noel Ambler
Pre AGM Meeting?	Yes, with Sharon Christensen, Independent Non-Executive Director, Chair of the People and Culture Committee and a member of the Audit and Risk Management Committee and Jatin Khosla, Head of Investor Relations.

Monitor Shareholding: An individual (or associate) involved in the preparation of this voting intention has a shareholding in this company.

Summary of issues for meeting

- Concerns about Giovani Rizzo's workload and small shareholding.

Proposed Voting Summary

No.	Resolution description	
1	Re-election of Giovani Rizzo as a Director	Undecided
2	Remuneration Report	For
3	Approve issue of STI Director Rights to Mike Veverka	For
4	Approve issue of LTI Director Rights to Mike Veverka	For
5	Approve increase to NED Fee Pool	For
6	Approve appointment of Ernst & Young as auditor	For
7	Approve renewal of Proportional Takeover Provisions	For

Summary of ASA Position

Consideration of accounts and reports - No vote required

Company overview

Jumbo Interactive (JIN) identify themselves as a “digital lottery specialist” which means they provide software and expertise for charity and government lotteries in Australia, UK and Canada.

The company has three operating segments. The share of group revenue is shown as a percentage.

- **Lottery Retailing.** 87%. Selling digital lottery tickets through the Oz Lotteries website and mobile app.
- **Software as a Service.** 8%. Developing and licensing a SaaS lottery management platform for use internally and with external customers. Branded as “Powered by Jumbo”.
- **Managed Services.** 5%. Providing a complete service to charities and worthwhile causes seeking to raise funds via lotteries.

In previous years Jumbo might have described themselves as a lottery reseller and this is still where the bulk of their revenue comes from. However, the annual report makes it clear that their goal is to diversify and build additional revenue streams.

Their market offers opportunities for growth. Digital sales currently represent 37% of the total domestic lottery market and are growing at 3% to 4% per year. The UK currently has 42% digital sales, and some Scandinavian countries are even higher.

Globally, the largest market for lotteries is the United States which is slowly adopting a digital model. Jumbo hopes to enter the US market in the future via a strategic partnership but, for now, their focus is on the Australian, UK and Canadian markets in that order.

Reporting Period Overview

Jumbo’s revenues are heavily influenced by large jackpots which attract new players and incentivise existing customers. In that regard, this has been a good year with 43 jackpots larger than $15m compared to 38 last year. Revenue was further boosted by a record $120 million Powerball in February, the first jackpot greater than $100 million since September 2019.

The company continues to grow through acquisitions: Gatherwell in the UK (2019), Stride in Canada (2022) and StarVale in the UK (settled in October 2022). These provide opportunities for growth by opening new territories, bringing in new lotteries and players and leveraging the “Powered by Jumbo” SaaS platform.

Governance and culture

Governance

Jumbo publishes a Corporate Governance Statement on their website which addresses each of the principles from the ASX Corporate Governance Principles and Recommendations.

They produce a board skills matrix but rather than showing each director's proficiency in a competency, it rates the Board's collective skills as either competent or expert. This does not let shareholders assess individual director skills. At the pre-AGM meeting, we suggested adopting a full disclosure matrix.

The company publishes a Core Values Statement and has policies in place for whistle blower, anti-money laundering, privacy, corporate governance, continuous disclosure, share dealing, anti-bribery and corruption.

Culture

Jumbo strives to create a flexible, engaging and rewarding environment for their employees. They operate as a "remote first" company with team members free to work wherever suits them including up to six months out of the year anywhere in the world.

They have been certified as a "Great Place to Work" and an "Employer of Choice" with 90% of employees agreeing with these accolades. Jumbo's employee engagement was 83%, which was ahead of an external industry benchmark of similar companies. 38% of vacant roles are filled by internal applicants.

Financial performance

The headline financial results look promising with Total Transaction Value (TTV) up 35.5% to $659m and revenue up 25.1% to $104m.

Revenue from the SaaS segment is up 68% to $8.3m and Managed Services is up 46% to $4.8m. These segments are growing more quickly than Lottery Retailing but are still dwarfed by its $91m revenue (up 21%). This SaaS revenue excludes fees paid by other segments for use of the Powered by Jumbo platform.

Expenses are up 30.8% or $8.6m which is mostly due to the tight market for skilled IT people and rising costs related to the company's growth such as marketing, recruitment, travel and insurance.

Cost of sales jumped by 73% to $14.4m driven by the service fee paid to The Lottery Corporation which increased from 1.5% to 2.5%. This will increase to 3.5% next financial year and 4.65% in FY24.

The increase in costs mean profits haven't increased to the same extent as revenue with statutory net profit after tax (NPAT) up 15.6% to $31m.

The traditional target dividend payout ratio of 85% of statutory NPAT is now a range of 65% to 85%. The intention being to retain some funds to pay down debt related to the StarVale acquisition. Having said that, the dividends for the year were at the traditional 85% ratio and were up 16% from last year.

The share price was down 20% to $14.22 at year end giving a TSR for the year of -17.7% compared to last year's +89.1%. Over the same period, the S&P/ASX 200 Net Total Return (ASX: XNT) showed a TSR of -6.1%.

The board has approved an on-market share buy-back of up to $25 million.

Key events

27 January 2022. Acquired StarVale, a UK external lottery manager and digital payments company, for 21.5m GBP (~$40.6m AUD). This will be funded from available cash and a bank facility of $30m AUD.

24 May 2022. Tabcorp's lottery and keno business was listed on the ASX as a separate company called The Lottery Corporation Limited. TLC is now the exclusive operator of licensed lotteries for all Australian states except for Western Australia. The demerger had no impact on Jumbo's agreement to resell tickets in these lotteries.

1 June 2022. Stride acquisition complete. Final payment of approximately $9m paid out of cash reserves. Stride made a one month contribution to financial results.

30 June 2022. Sold Lightning Payroll, a non-core software development and licensing business, for $800k.

12 October 2022. UK Gambling Commission approval was received for the StarVale transaction.

Key Board or senior management changes

1 July 2022. Richard Bateson left the Executive KMP. He transitioned from Chief Commercial Officer to International Lottery Advisor reporting to the CEO.

26 August 2022. Abby Perry joined the Executive KMP. She is Jumbo's first Chief People Officer (CPO) and will oversee human resources and people operations across the organisation.

ASA focus issues (not discussed elsewhere in this report)

Cybersecurity

Jumbo collects, uses and stores data on their partners and their customers, including account, card-holder and transactional data.

A materiality assessment of significant risks highlighted data protection, privacy, cyber risk and security as the most important and impactful risks the company faces.

A Data Breach Notification Policy and a response plan are in place. No reportable data breaches occurred in FY22. They have rigorous IT security processes including penetration testing and threat simulations. They have adopted an enhanced cybersecurity posture in response to the Australian Cyber Security Centre (ACSC) recommendations.

Jumbo audits the PBJ SaaS platform annually to maintain the ISO27001 Information Security Management System certification. They have been certified as compliant with the Payment Card Industry Data Security Standard (PCI-DSS) which is aimed as safeguarding credit and debit card information.

Sustainability

The company published its first Sustainability Report in FY22 and established a Sustainability Council which reports to the board each month.

They prepared a carbon baseline for FY19 and plan to conduct an FY22 assessment next year. The intention is to set a post COVID-19 benchmark against which future improvements can be measured.

Jumbo produces no scope 1 emissions, and they have clear targets and timeframes for reducing scope 2 & 3 emissions. The goal is for Australian operations to be carbon neutral through offsets by FY23 and net zero through reductions by FY26. With international operations shortly after that.

Their supply chain is low risk with predominantly information, communications and technology suppliers based in low-vulnerability countries. They plan to issue a Modern Slavery Statement for FY22 by 31 December 2022.

Jumbo operates in the gambling sector which has attracted a lot of attention recently. Lotteries generally are far less harmful than other gambling formats, and charity lotteries are the least risky form of lottery. Jumbo takes responsible gambling very seriously and has multiple safeguards in place to protect their players from risky behaviour.

Diversity

Jumbo has a commitment to pay equity, inclusion, and gender and cultural diversity. They collect and publish data on many different aspects of diversity and have a calendar of events to celebrate diversity.

Their gender equity goal is to achieve a 40:40:20 ratio for Board, Senior Leadership Group (SLG) and at the Group level by the end of FY26. Currently female representation is 50% on the board, 20% SLG and 47% for the group. While it is encouraging to see Abby Perry promoted to a C-level executive role, the number of females in the SLG has dropped from five in FY21 to four in FY22 because one of the roles previously held by a female was not replaced.

In the pre-AGM meeting, we discussed the proactive steps the company is taking to meet its goal of 40% female senior leadership by 30th June 2026.

The company plans to implement a Reconciliation Action Plan by November 2022.

Summary

(As at FYE)	**2022**	**2021**	**2020**	**2019**	**2018**
NPAT ($m)	31.17	26.96	25.88	26.42	12.13
UPAT ($m)	32.20	28.35	26.46	26.42	11.75
Share price ($)	14.22	17.77	9.58	20.15	5.00
Dividend (cents)	42.5	35.0	35.5	36.5	18.5
Simple TSR (%)	-17%	89%	-52%	294%	90%
EPS (cents)	51.5	45.4	42.0	42.5	21.9
CEO total remuneration, actual ($m)	1.518	1.390	1.301	1.315	0.972

Re-election of directors

Gionvanni Rizzo has been on the board since 1st January 2019 and is seeking re-election as a non-executive director. Mr Rizzo is a specialist in the gaming industry with over 20 years' experience in various roles. His skills and experience are a valuable addition to the Jumbo board as he is the only member, besides the CEO, to have first hand work experience in the gambling industry. ASA has two concerns about his re-election: workload and shareholding.

Workload. Mr Rizzo is also Chief Investor Relations Officer at Tyro Payments which is entering a potentially busy period with a class action and takeover requiring attention. While Mr Rizzo's record to date shows he can juggle multiple roles we would like to question him on the potential increase in workload.

Minimum shareholding. At the time of the AGM, Mr Rizzo will have been on the board for almost four years. Jumbo NEDs have a minimum shareholding requirement of 100% of their fees within five years of their appointment date. ASA prefers a three year deadline.

Mr Rizzo holds 2,000 shares which at the end of financial year share price represented just 23% of his NED fee. This is the lowest percentage of anyone on the board or in the senior executive. In fact, Mr Rizzo's percentage has been going backwards as his fees increased but his holdings remain static.

Noting that he still has time under the Jumbo five year deadline, ASA would like to ask Mr Rizzo how he intends acquiring the almost $100k of shares he needs within the mandated timeframe.

ASA will raise both topics with Mr Rizzo at the AGM and will make a decision on his re-election based on his response.

Adoption of Remuneration Report

In the last few years, ASA raised concerns about some aspects of the company's remuneration framework and, although it has improved, some of those concerns remain. A new framework will be in place for FY23 which is better aligned with the ASA guidelines (with some deviations as described in the appendix). We note Jumbo is outside the top 200 companies and our guidelines apply in full to the larger companies

The board used its discretion to award that part of the STI associated with the StarVale acquisition even though it did not receive regulatory approval until early October 2022. This does not meet with ASA expectations, and while it seems appropriate the executives should not be punished for administrative delays it should be noted that shareholders did not receive any benefit during the three month delay.

On balance, ASA approves of the remuneration report and looks forward to the FY23 changes so will vote in favour of this resolution.

Issue of STI & LTI Director Rights to the CEO

This resolution relates to granting short and long term incentive rights to the CEO, Mike Veverka. Because the CEO is also a director, shareholder approval must be obtained to grant these rights. ASA is comfortable with the remuneration framework although we would prefer the rights were purchased on market rather than issued.

ASA will vote in favour of these resolutions.

Increase to non executive director fee pool

Shareholders are being asked to approve an increase in the pool from which non executive director fees are paid from $750K to $1m. The current pool was set by shareholders in 2019. It is important to note that this pool increase does not mean the directors will get an immediate pay rise, although that is a possible future outcome.

The notice of meeting states the board is seeking shareholder approval to increase the NED fee pool to allow additional NEDs to be appointed to the Board (if required); and maintain remuneration arrangements that are market competitive. There is no suggestion that a new NED appointment is imminent.

We sought further clarity on the rationale at the pre-AGM meeting. The Jumbo board is small, and it is likely additional directors will be added in the future. The company wishes to have the financial capacity to attract the best possible candidates. It is likely that one or more of these new directors will be from overseas. Overseas appointments may require higher remuneration than Australian NEDs and the issue of foreign exchange risk must be considered. The board wishes to add enough head room to the pool to accommodate all possible outcomes for the next three years.

ASA has access to remuneration market research from Godfrey Remuneration Group which shows the current pool is below the median, $900k, of other companies with a similar market capitalisation. The research also shows that after this year's 13% increase for the chair and 25% for the NEDs, their remuneration is higher than the market average. Jumbo's external research suggests the director fees are average when viewed on a per diem basis.

ASA is satisfied that the fee pool increase is justified and intends voting for the resolution.

Appointment of Ernst & Young as auditor

The previous auditor (BDO) has resigned and Jumbo wishes to replace them with Ernst & Young. Neither the annual report nor the notice of meeting mentions the reason for BDO's resignation. In a pre-AGM meeting it was explained that BDO had been the company's auditor for 15 years and the board thought it was good practise to consider their options. The auditor role was put out to tender and the proposal from Ernst & Young was successful. BDO's resignation is just an administrative formality.

ASA will vote in favour of the new auditor appointment.

Renewal of Proportional Takeover Provisions

A proportional takeover is where a predator only bids for a proportion of a shareholders' interest. The ASA prefers full takeovers so that shareholders are not left with a minority stake in a company controlled by the predator.

The provisions require majority shareholder approval for a proportional takeover. Such provisions need to be approved by shareholders every three years and in Jumbo's case this occurred in 2010, 2013, 2016 & 2019.

ASA will vote in favour of this resolution.

Appendix 1
Remuneration framework detail

CEO rem. Framework for FY22	Target* $k	% of Total	Max. Opportunity $k	% of Total
Fixed Remuneration	800	50%	800	50%
STI - Cash	200	12.5%	200	12.5%
STI - Equity	200	12.5%	200	12.5%
LTI	400	25%	400	25%
Total	1,600	100%	1,600	100%

The amounts in the table above are the 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.

Executive remuneration for FY22

The executive remuneration framework for FY22 has the following components.

- Fixed remuneration (FR). 50% of total remuneration is paid as base salary and superannuation. This is not at risk.
- Short term incentive (STI). 25% of total remuneration is subject to performance hurdles. STI is 50% cash and 50% equity deferred for two years.
- STI hurdles relate to underlying net profit after tax (NPAT), total transaction value (TTV), group earnings and specific milestones such as acquisitions.
- Long term incentive (LTI). 25% of total remuneration is subject to the JIN share price outperforming the ASX 'total return' All Ordinaries index. STI is 100% equity and is granted at the end of a three year performance period.
- Minimum shareholding requirement (MSR). Executives must hold 100% of their total remuneration opportunity (FR + STI + LTI) within five years of falling under the remuneration framework.

Most of the STI hurdles were met with the exception of entering the US market and settling the StarVale acquisition. The Board determined the StarVale acquisition was effectively complete and is only waiting for regulatory approval and used its discretion to pay that part of the STI.

The NPAT hurdle uses a sliding scale where a 6% NPAT increase yields 10% of max STI up to a 20% increase which yields 100%. NPAT increased by 14% this year resulting in 70% of target being paid.

The CEO's total remuneration for the financial year was $1,518,984 including fixed remuneration, cash bonus, superannuation, leave, options and rights.

Changes to executive remuneration for FY23

The remuneration framework will be modified in FY23. The major changes are as follows.

- A second LTI hurdle will be introduced, and the hurdles will be better aligned with the creation of shareholder value. Metrics will be relative TSR and underlying EPS growth
- STI hurdles will include metrics for financials, sustainability, customer, employee and an individual performance evaluation.
- STI hurdles will include a “financial gateway” which must be met before the non financial hurdles can be tested.
- The STI & LTI schemes will be expanded to include all members of the Senior Leadership Group.
- Independent benchmarking of Executive KMP remuneration found the fixed component to be below market average having not increased for the past two years. The board approved an increase, but it was deferred for a year in light of the economic uncertainty.

These changes are mostly positive from ASA’s perspective and the proposed remuneration framework aligns well with our guidelines. However, there are still some deviations as follows.

- LTI rights are exercisable into shares after three years where the ASA prefers four or five.
- TSR comparison is the ASX ‘total return’ All Ordinaries index (XAOA:ASX) rather than a basket of companies from similar industries and including key competitors and any relevant foreign companies.
- LTI can still be paid even if absolute TSR is negative.
- New shares are issued for STI & LTI rather than being bought on market.

Board remuneration for FY22

The chair receives a salary of $213k and NEDs receive $125k. This represents an increase from last FY of 13% for the chair and 25% for the NEDs. Additional fees are paid for committee membership.

ASA has access to market remuneration research from Godfrey Remuneration Group which shows the chair and NED fees are high compared to their peers. The chair being about 5% above average and the NEDs about 15%.

Jumbo’s external research suggests the director fees are average when viewed on a per diem basis.

Minimum shareholding requirement

Two directors and one executive are yet to reach their minimum shareholding requirement of 100% of their total remuneration opportunity.

- Sharon Christensen = 40%
- Giovanni Rizzo = 23%
- Brad Board = 71%

None of the three have reached Jumbo's five year accumulation deadline so there is still time for them to reach the MSR. However, ASA prefers a three year deadline which Mr Rizzo and Ms Christensen will have exceeded by the time of the AGM.

Brad Board (COO) added 15,628 shares during the financial year, but Sharon and Giovanni did not increase their holdings. It is worth noting that Xavier Bergade (CTO) received another 307,599 shares due to exercising rights giving him more skin in the game than anyone on the board or KMP with the exception of the CEO.