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New Chair and CEO, Growth Continues

Company/ASX Code	Metcash Limited / MTS
AGM date	Wednesday, 7 September 2022
Time and location	2:30 pm, King Room, Hyatt Regency, 161 Sussex St, Sydney
Registry	Boardroom
Type of meeting	Physical, telephone listening
Poll or show of hands	Poll on all items
Monitor	Don Adams assisted by Gary Barton
Pre-AGM Meeting?	Yes, online meeting with new Chairman Peter Birtles, NED Helen Nash (previous Chair of People and Culture Committee), NED Margaret Haseltine (incoming Chair of People and Culture Committee) and Steven Ashe (GM Corporate Affairs & Investor Relations).

One individual involved in the preparation of this voting intention has a shareholding in this company.

Summary

While growth was slower than in FY 2021 it was still solid with Revenue up 6.4% to $17.4bn and EBIT up by 17.7% to $472m. The CEO and Chairman have both retired and Metcash has satisfactory replacements. The Remuneration Report still has some of the problems identified last year, but it has improved, and we shall vote for it.

Proposed Voting Summary

No.	Resolution description	
2(a)	Election of Mr Mark Johnson as a Director	For
2(b)	Re-election of Mr Peter Birtles as a Director	For
2(c)	Re-election of Ms Helen Nash as a Director	For
3	Adoption of Remuneration Report	For
4	Approval of grant of performance rights to CEO/Managing Director Mr Douglas Jones	For

Consideration of accounts and reports - No vote required

Governance and culture

Metcash has a well-structured Board and has managed the transitions to a new Chairman and CEO (see discussion below) with style. In addition to the material in the Annual Report they have published substantial Governance and Sustainability reports. The company has adopted firm targets for environment and diversity achievements.

The Board Skill Matrix in the Governance statement was confusing. It failed to identify which directors have which skills, as we would prefer. In discussion it emerged that they claimed that practically all directors had all of the many skills listed.

Last year the AGM approved an increase in the pool of funds for directors' fees and there have since been small increases (less than 5%) in fees paid. Also, all directors (except for the new appointee Mark Johnson) have enough shares to cover one year's fees. It helps that the share price has increased so much.

Financial performance

Revenue growth of 6.4% varied markedly among the three pillars that make up Metcash' business. Food revenue grew by only 1.4% to $9.5bn an apparent decline in real terms. The company pointed out that the wholesale price index for the goods sold to the franchisees, excluding produce and tobacco, was up by only 0.5% over the period.

Hardware sales, on the other hand, were up 20.5% to $3.1bn reflecting double digit growth in all areas as well as the impact of acquisitions. Liquor sales increased by 8.7% to $4.8bn.

Metcash continues to push its MFuture and Project Horizon initiatives which are aimed at major revamping of the technology base of the business. In FY2022 these cost $35m which was treated as significant items. This is the substantial part of the $54m difference between UPAT and NPAT shown in the Summary table below.

The Balance Sheet is strong, the share price has grown with a TSR of 40.6% and dividends were up 23% to 21.5 cents per share.

Board and Management Changes

In July 2022 it was announced that the Chairman of Metcash, Rob Murray, has resigned effective 1 August 2022 and has been replaced by Peter Birtles. Mr Birtles joined the Board on 1 August 2019. Apparently, Mr Murray's intentions had been known for some time. A new director, Mr Mark Johnson was appointed to the Board on 1 August as well.

Metcash CEO Jeff Adams also retired and on 11 March 2022 was replaced by Doug Jones who had joined on 1 February. Mr Jones spent the last 14 years as a senior executive with a South African company, Massmart, which is majority owned by Walmart Inc. Prior to that he had worked in Canada. We queried Mr Jones lack of Australian experience and were assured that his recruitment was the result of an extensive international search and that his personal qualities make him an outstanding choice.

Summary

(As at FYE)	2022	2021	2020	2019	2018
NPAT ($m)	245.4	239.0	(56.8)	192.8	(148.2)
UPAT ($m)	299.6	252.7	198.8	210.3	216.9
Share price ($)	4.79	3.55	2.49	2.87	3.60
Dividend (cents)	21.5	17.5	12.5	13.5	13
Simple TSR (%)	40.6	48.4	(8.9)	(16.5)	73.5
EPS (cents)	25.0	23.4	(6.2)	20.8	(15.2)
CEO total remuneration, actual ($m)*	6.01*	5.25	3.21	3.67	4.12
*CEO total remuneration for 2022 includes $5.57m for Mr Adams (retiring) and $0.44m for Mr Jones (new CEO).					

Election or re-election of directors

There are three directors up for election or re-election. That are all well qualified with extensive relevant experience and we intend to vote for each of them.

First is the election of **Mark Johnson** who was appointed to the Board on 1 August 2022 to fill the vacancy left by Rob Murray's resignation. He has strong experience in finance and as a non-executive director. He is currently a NED of four other companies: Boral, Goodman Group, HCF and Aurecon.

Next will be the vote to re-elect the new Chairman **Peter Birtles** as a director. He has been on the Metcash Board since 2019 and we were impressed when we met him recently.

The last re-election is for **Helen Nash** who has been a director since 2015. She has been Chair of the People and Culture Committee and we have met her in that role. She has recently moved into a new role as Chair of the Audit, Risk and Compliance Committee.

Adoption of Remuneration Report and approval of equity grants to Managing Director/CEO

We intend to vote proxies for the Remuneration Report and equity grant motions. There is a more complete analysis in the attached Appendix. While the Remuneration Report is clearer than last year, the policy is virtually identical. Also, the remuneration structure for the new CEO is virtually the same as the previous CEO's.

There were two exceptional performance rights grants made during the year. A Buy-Out Grant of $1.2m to the new CEO Doug Jones to partially compensate him benefits he lost by leaving his previous employer and a Retention Grant of $1m in performance rights to the CEO Food Scott Marshall since he was not successful in getting the overall CEO Job. There is more discussion in the Appendix.

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Appendix 1
Remuneration framework detail

Here is the compensation structure for the new CEO, Doug Jones. It is quite close to the compensation structure for the previous CEO, Jeff Adams, with slightly lower Fixed Remuneration and higher LTI.

CEO rem. Framework for FY22	Target* $m	% of Total	Max. Opportunity $m	% of Total
Fixed Remuneration	1.750	48%	1.750	30%
STI - Cash	0.817	22%	1.838	31%
STI - Equity	0.408	11%	0.919	15%
LTI	0.700	19%	1.400	24%
Total	3.675	100%	5.906	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.

Remuneration policy is generally sound and the presentation in the FY2022 Annual Report is somewhat clearer than the previous year's explanation.

STI is calculated in two steps. First, the STI opportunity is scaled by EBIT with 100% available if EBIT reaches budget and 150% if EBIT is 105% of budget. The next step is to review ten performance measures: Sales revenue, UPAT, EBIT, ROFE, Cash conversion, Project Horizon, Safety, Engagement, Business Metrics and MFuture program. There is only limited detail in the remuneration report as to how these are used. For example, what weighting applies to each outcome in calculating STI.

STI awards are 67% cash and 33% in performance rights which are not vested until the following year.

LTI awards are based on a three-year performance period and use ROFE and TSR measures. Full vesting occurs if ROFE exceeds 26% and if compound TSR exceeds 10% p.a. All equity awards are subject to clawback for cause.

Other Grants

During the year Metcash has made two significant grants of performance rights, a Buy-Out Grant to the new CEO, Doug Jones and a Retention Grant to the CEO of the Food Pillar, Scott Marshall.

The Buy-Out Grant of $1.2m of performance rights at then market value was to compensate Mr Jones for pay-outs he forfeited by leaving his previous employer in South Africa. We were told that the amount of the grant is less than the amount forfeited. The grant will vest in two equal tranches in 2023 and 2024 subject to EBIT targets, service conditions and Board approval.

A buy-out payment like this is not unusual, and it is good that Metcash are not paying cash but have structured it as conditional vesting based on achievement. On the other hand, they are not seeking shareholder approval for the equity grants as is generally required for grants to a Board member. We were told that this was because they were buying the shares on the market and not issuing new equity. It may also be that negotiations with the new CEO required that the grant be made before the AGM. The ASA would prefer shareholder approval for all equity-based compensation for the CEO, including the equity component of STI.

The Retention Grant of $1m of performance rights to the CEO Food, Mr Marshall, will vest in three annual tranches subject to a service condition, EBIT targets and Board assessment of his performance and behaviour. The Chairman explained to us that Mr Marshall was the leading internal candidate for the CEO role, that they highly value the job that he is doing, and that the grant was to encourage him to stay with Metcash. Shareholder approval is not normally sought for grants to executives who are not Board Members.

In particular, the Chairman told us that Mr Marshall maintains excellent relationships with the franchisees who run the stores. Some years ago, relations had been tense, and it is an important strategic objective for Metcash to maintain good relationships. He also commented that Mr Jones, since becoming CEO, was also establishing good connections with the retailers.

Voting intention

The ASA has the following problems with the Remuneration Report:

1. The STI criteria are complex and confusing.
2. Shareholder approval is not being sought for the STI equity allocation to the CEO, nor for the Buy-Out Grant.
3. We prefer that at least 50% of STI be deferred equity, but Metcash only defers 33%.
4. We prefer a period longer than three years for vesting of LTI awards.

Last year we voted for the Remuneration Report, but there has only been a slight improvement since then. Nevertheless, we will vote proxies for this motion. The company is aware of our views, and we expect that policy will improve in the future.