



**Upside of the cycle – a strong year plus \$780m in one-off windfalls**

<b>Company/ASX Code</b>	BlueScope Steel (BSL)
<b>AGM date</b>	Friday 23 November 2018
<b>Time and location</b>	10am Intercontinental Sydney, 117 Macquarie Street, Sydney
<b>Registry</b>	Link
<b>Webcast</b>	Yes
<b>Poll or show of hands</b>	Poll on all items
<b>Monitor</b>	John Whittington assisted by Mike Robey
<b>Pre AGM Meeting?</b>	Yes with Chair John Bevan

<b>Item 1</b>	<b>Annual Report</b>
<b>ASA Vote</b>	No vote required

**Summary of ASA Position**

**Financial performance**

In financial year 2018 (FY18), BlueScope’s revenue increased 9% to \$11,526m, principally due to higher steel prices in all regions, increased sales volumes in the Australian steel products segment, and the effect of a stronger Australian dollar exchange rate. 37% of revenues came from Australia, 35% from North America, and 20% from Asia.

Reported net profit after tax (NPAT) for the year was \$1,569m (up 119%) which was helped by gains due to adjustments in tax liabilities of about \$500m, writebacks of previous impairments of about \$200m, and benefits from US corporate tax cuts of \$76m. Excluding these figures, underlying NPAT for the year was \$826m (up a very respectable 27%).

Cash flow from operations was fairly steady at \$1,141m and free cash flow was down 2% to \$731m.

Dividends increased 55% to 14 cents per share and total shareholder return for the year was 31.5% (30.7% from the increase in share price and 0.8% from dividends). Return on equity was 15.3% (up from 13.5% last year; it was below 2.1% in all years between 2009 and 2014).

**Key events**

The company completed a \$300m buy back in FY18 and has announced a \$250m buy-back for first half FY19.

## **Key Board or senior management changes**

Long standing CEO Paul O'Malley retired on 31 December and was replaced by Mark Vassella who previously headed BlueScope's Australian and New Zealand operations. Post year-end, Mark Hutchinson was appointed a director on 1 October 2018.

## **ASA focus issue**

Remuneration disclosure is good but lacks a table of actual remuneration. Director and senior executive equity holdings are good and shareholder participation seems satisfactory. The board is 33% female, 67% male.

## **Summary**

(As at FYE)	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
NPAT (\$m)	1,569	716	354	136
UPAT (\$m)	826	652	307	161
Share price (\$)	17.26	13.21	6.37	3.00
Dividend (cents)	14	9	6	6
TSR (%)	32%	109%	114%	-44%
EPS (cents)	282	125	62	24
CEO total remuneration, <u>reported</u> (\$m)	3.849	6.863	7.529	4.371

For 2018, the CEO's total reported remuneration was **45 times** the Australian Full time Adult Average Weekly Total Earnings (based on May 2018 data from the Australian Bureau of Statistics).

<b>Item 2</b>	<b>Adoption of Remuneration Report</b>
<b>ASA Vote</b>	<b>For</b>

## **Summary of ASA Position**

The presentation of the remuneration report is good with a clear and understandable outline of remuneration structure and good disclosure of performance targets and achievements. However, unlike many of its peers it does not include a table of actual remuneration.

The remuneration structure has been changed from previous years with the (new) CEO's fixed remuneration reduced by 15% and reduced short-term (STI) and long-term (LTI) incentives.

The STI, which can range from 0% of fixed remuneration to 67% of fixed remuneration for the CEO (53% for other key management personnel (KMP)), provides a bonus based 55% on company financial metrics (underlying return on invested capital (ROIC), free cash flow, and safety) and 45% on personal achievement of strategic objectives.

LTI, which the company now calls alignment rights and can range from 0% of fixed remuneration to 100% of fixed remuneration for the CEO (66% for other KMP), have been paid on relative total shareholder return (RTSR) and earnings per share (EPS) growth rate in the past but this will change in the new plan.

More details on STI and LTI targets and calculation are discussed below under items 4 and 5.

We note that BlueScope use underlying metrics for both STIs and LTIs however the adjustments are highly transparent and seem reasonable given the cyclical nature of the business and the significant one-off gains from accounting adjustments (around \$700m this year alone) which are excluded from incentive calculations.

We intend to support the remuneration report.

<b>Item 3</b>	<b>Election of Mr Mark Hutchinson as a Director</b>
<b>ASA Vote</b>	<b>For</b>

#### **Summary of ASA Position**

Mr Hutchinson, who previously held senior executive positions at General Electric in a 25-year career with the company, was appointed to the board on 1 October 2018. He already has a shareholding equivalent to about 75% of his anticipated total remuneration and independent.

Mr Hutchinson holds no other listed company directorships. We do not consider his workload excessive.

We believe that Mr Hutchinson is well qualified, is likely to contribute to the board, and we support his election.

<b>Item 4</b>	<b>Approval of grant of Share Rights to Mark Vassella under the Company's Short-Term Incentive Plan</b>
<b>ASA Vote</b>	<b>For</b>

#### **Summary of ASA Position**

This is for the issue of a maximum of 67,038 share rights worth about \$933,000 (based on the share price as at 26 October). This is equivalent to 52% of base salary (it was worth 67% at the time of issue) and has been calculated based on face value.

The specific measures have not been disclosed yet, but the FY 2018 measures were safety, cash flow, underlying ROIC, and personal achievement of strategic objectives. Disclosure of actual achievement was good.

If performance is below the threshold then no rights will vest, if performance is between the threshold and the maximum then a linear scale will apply from 33% vesting at the threshold to 100% vesting at the maximum. If performance is above the maximum, then all rights will vest.

There is no holding lock on these shares, so they can be sold at any time once vested. The Board has discretion to determine that rights lapse for misconduct (clawback is also possible) and rights will lapse on termination for cause or resignation.

On balance we believe the awards are not excessive, are aligned with shareholder value and are highly transparent and well explained, so we intend to support the resolution.

<b>Item 5</b>	<b>Approval of grant of Alignment Rights to Mark Vassella under the Company's Long-Term Incentive Plan</b>
<b>ASA Vote</b>	<b>For</b>

### Summary of ASA Position

This is for the issue of a maximum of 100,557 alignment rights worth about \$1.4m (based on the share price as at 26 October). This is equivalent to 78% of base salary (it was worth 100% at the time of issue) and has been calculated based on face value.

The rights will vest fully if two criteria are achieved. These criteria are underlying earnings before interest and tax ROIC over the period 1 July 2018 to 30 June 2021 to be greater than 10%, and the ratio of the average annual leverage calculated at six monthly intervals over the period 1 July 2018 to 30 June 2021 to be less than one.

If one or both of the performance criteria is not satisfied, then all the alignment rights will lapse. The Board has discretion to determine that rights lapse for misconduct (clawback is also possible) and rights will lapse on termination for cause or resignation.

We have some concerns that total shareholder return (TSR) is no longer used for LTIs however in discussion with the Chair we understand that for a cyclical industry stock such as BlueScope which can experience 10% price changes in a day they feel TSR is an unreliable incentive for management. He also pointed out that as BlueScope would probably outperform all other listed steel companies, a RTSR measure against peers would always be met. BlueScope believes that in such a market this is all handled better by their KMP shareholding requirements (100-200% of fixed pay for CEO, 50-100% of fixed pay for other KMP).

On balance we believe the awards are not excessive, are aligned with shareholder value and are highly transparent and well explained, so we intend to support the resolution.

<b>Item 6</b>	<b>Approval of Potential Termination Benefits</b>
<b>ASA Vote</b>	<b>For</b>

### Summary of ASA Position

BlueScope believes that the Corporations Act provisions regarding termination benefits greater than twelve months applies to not only KMP but all directors of all BlueScope subsidiaries in its 18 different geographies. BlueScope gave the example of Belgium where the local law mandates termination benefits in excess of 12 months.

Hence the need for this item which gives approval for the company to allow share rights to vest upon termination or death or disability of employees. Similar resolutions were passed at the 2010 and 2015 AGMs and supported by the ASA. This item seeks to update the approvals effective for a period of 3 years now that changes have been made to the incentive plans and gives the board discretion to determine the most appropriate termination package in accordance with the relevant employment agreement and the share incentive plan rules.

ASA generally opposes pre-approval of termination benefits which exceed 12 months fixed pay except where payment of vested STI or LTI awards are likely to push a termination payment in excess of the 12-month limit. As these criteria apply in this case then we will support the resolution.

The individual(s) (or their associates) involved in the preparation of this voting intention have no shareholdings in this company.

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