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Coles Group – Bigger than Newcastle

Company/ASX Code	Coles Group
AGM date	Thursday 5 November 2020
Time and location	10:30am, Virtual at https://web.lumiagm.com/310816539
Registry	Computershare
Webcast	Yes
Poll or show of hands	Poll on all items
Monitor	Stewart Burn assisted by John Whittington
Pre AGM Meeting?	Yes with Chair James Graham and Richard Freudenstein

John Whittington has been involved in the preparation of this voting intention and has a shareholding in this company.

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

Summary of ASA Position

This is the first full year that Coles Group has reported following its spin-off from Wesfarmers. Considering the difficulties in the sector associated with the pandemic, it did very well reporting sales revenue growth of 6.9% compared to 3.2% in 2019 up to $37.4bn, declaring a total dividend of 57.5c compared to 35.5c, which represents an 82% payout. All seven NEDs have had line management responsibility in areas related to Coles with the CEO Steven Cain now having been in his position for well over a year. Coles has developed a strong governance culture as set out in their report.

Coles Group is focused on Supermarkets (88% of total revenues), Liquor (8.8% of total revenues) and Express (3.2% of total revenues). This year new initiatives were undertaken in Coles Online, support of indigenous communities, community support and direct milk sourcing, this and issues associated with the pandemic has resulted in the group creating 10,000 new jobs this year. The Group reported a strong start to FY21 with supermarket sales broadly in-line with levels achieved in the second half of FY2020. Associated with the pandemic and especially in Victoria online sales jumped more than 60% and now represent 6% of total sales and the first year it has made a profit. Coles Group now see online sales as being an integral part of their future and have recently appointed Ben Hassing in this area, who used to run Walmart in China. The Group did experience significant difficulties in the Express area associated with low foot traffic and we note that the performance of its Liquor business was not as good as its competitors, however; the Group believes the appointment of Darren Blackhurst will address this sector.

Summary

(As at FYE)	**2020**	**2019**
NPAT ($m)	$978	$1,434
UPAT ($m)	$951	$1,078
Share price ($)	$17.15	$13.35
Dividend (cents)	57.5	35.5
TSR (%)	31	6.9
EPS (cents)	73.3	80.8
CEO total remuneration, ***statutory*** ($m)	$4.85	$5.4

For 2020, the CEO's total statutory remuneration was 54 **times** the Australian Full time Adult Average Weekly Total Earnings (based on May 2019 data from the Australian Bureau of Statistics).

Item 2.1	**Election of Paul O'Malley as a Director**
ASA Vote	**For**

Summary of ASA Position

Paul O'Malley became a non-executive director (NED) of Coles on 1 October 2020 and will be Chairman of the Audit and Risk Committee and a member of the Nomination Committee. He currently holds 3809 shares in Coles Group. Mr O'Malley is a director of Commonwealth Bank of Australia Limited (since 2019) and he was Managing Director and Chief Executive Officer of BlueScope Steel Limited from 2007 to 2017. He was previously the Chief Executive Officer of TXU Energy, a subsidiary of TXU Corp based in Dallas, Texas. Mr O'Malley is a former director of the Worldsteel Association, Chair of their Nominating Committee and trustee of the Melbourne Cricket Ground Trust. Mr O'Malley currently serves as the Chairman for Australian Catholic Redress Ltd. He appears to have significant experience with companies of the size of Coles Group but not in retailing, so it is difficult to see the value he adds to the board. He was highly recommended by the board and his workload does not exceed that recommended by the ASA. The ASA has no objection to his re-election, recognising how difficult it can be to find talented people.

Item 2.2	**Re-election of David Cheeswright as a Director**
ASA Vote	**For**

Summary of ASA Position

David Cheesewright has been a non-executive director since November 2018 and currently owns 20,000 shares. He has significant experience in retailing having retired in early 2018 as President and Chief Executive Officer of Walmart International, which comprises Walmart's operations outside the United States. Mr Cheesewright was also responsible for Walmart's global sourcing operations and offices around the world. He was previously President and CEO of Walmart EMEA (Europe, Middle East and Africa), CEO of Walmart Canada, and COO of Asda. Mr Cheesewright's other prior roles include a range of key positions with Mars Confectionery in the UK across manufacturing, marketing, sales and logistics.

He appears to have a skill set that is valuable to the board, has a suitable workload and the ASA supports his re-election.

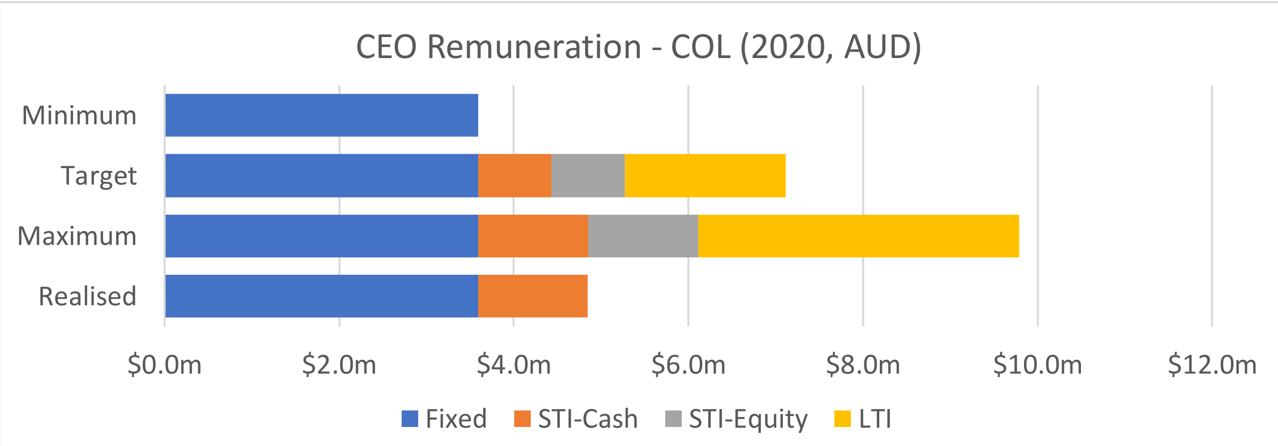
Item 2.3	**Re-election of Wendy Stops as a Director**
ASA Vote	**For**

Summary of ASA Position

Wendy Stops has been a non-executive director since November 2018 and owns 20,000 shares. She has been a director of Commonwealth Bank of Australia Limited (CBA) since 2015 and will be retiring at the conclusion of CBA's AGM, so should have more time to devote to Coles. She is also a director of Fitted for Work, a Council member at the University of Melbourne, Chair of the Advisory Board for the Melbourne Business School's Centre for Business Analytics and a member of the Advisory Committee to the Digital Technology Taskforce of the Department of Prime Minister and Cabinet. She has significant experience in IT, so should provide value as Coles moves to a more online presence.

She appears to have a skill set that is valuable to the board and the ASA supports her re-election.

Item 3	**Adoption of Remuneration Report**
ASA Vote	**For**



Source: Australian Shareholders' Association and company 2020 Annual Report, realised STI & LTI are from prior years

Summary of ASA Position

The remuneration report is generally compliant with ASA guidelines, however; it was rather difficult to calculate the actual remuneration as it only gives details on some of the actual remuneration amounts, ie short term incentives (STI) and long term incentive (LTI) performance share remuneration. We have raised this issue with Coles group and given examples of good practice, so hopefully it will be clearer next year. The details given for calculating fixed remuneration and STI for 2020 were clear and reasonable and the issues raised last year have been addressed, especially with regards to the inclusion of a total shareholder return (TSR) component. It is understood that a large cash payment of $1,506,776, for other benefit costs will not be paid next year as the base total fixed compensation (TFC) component will reduce to $2.1M as detailed in the notice of meeting. We will monitor this issue for next year. According to the Godfrey Remuneration Group (GRG) a company of size of Coles Group would pay its CEO in the vicinity of $6M at the 50th percentile, thus Mr Cain's total package this year is not excessive. This will be monitored in future years as the STI and LTI performance shares vest. All NEDs have a shareholding that exceeds one year's fees, although the CEO still does not have a shareholding equal to his remuneration, only holding 50,000 shares at the end of the financial year. This is expected to be addressed in future years as the share-based components of the STIs and LTIs are awarded. For STIs performance is measured against Group earnings before interest and tax (EBIT), Group sales and Group cash realisation. Non-financial measures contribute up to 40% of the STI opportunity for the CEO. It is proposed that online retailing will be included as a component of this for 2021. We did suggest that net profit after tax (NPAT) may be an item that should be considered. For LTIs, 50% are subjected to a return on capital (ROC) hurdle and 50% to a TSR hurdle. The ROC hurdle is considered commercial in confidence. The TSR hurdle vests 50% at the 50th percentile, with straight line vesting to the 75th percentile, where 100% of shares are vested. Currently the LTI performance shares are vested after 3 years rather than the preferred 5 years period of the ASA. This issue has been raised with Coles. We will monitor this position on an on-going basis. ASA supports the remuneration report.

Item 4	**Approval of STI grant of performance rights to the MD and CEO**
ASA Vote	**For**

Summary of ASA Position

For 2020 the STIs for executive key management personnel (KMP) were 80% of Total Fixed Compensation (TFC) at target and 120% of TFC at maximum. With 50% of STI to be paid as cash and 50% as shares (75,866) restricted for 2 years. Whilst we did question the almost full payment of the STI at 119% of 120% due to the gains Coles Group made from the pandemic, we were assured that the Group was on target to achieve stretch and above stretch before the pandemic hit. We did observe that Mr Cain's TFC for calculating the STI will reduce to $2.1M next year compared to $3.6M this year. With the additional issues Coles Group faced during the pandemic and the fact that he has delivered on a number of new initiatives, we agreed with the board that he was eligible for the STI as indicated. The ASA supports this resolution.

Item 5	**Approval of long-term incentive grant of performance rights to the MD and CEO**
ASA Vote	**For**

Summary of ASA Position

For 2020 the LTIs for the KMP would be 175% of TFC for the CEO and 150% of TFC for other KMP, with 50% of the LTI subjected to an ROC hurdle and 50% subjected to an TSR hurdle. The ROC component only vests if more than 95% of the of the cumulative ROC targets are met, as these are set by the board, we do not know if they are fair and reasonable and will continue to monitor this in future years. The TSR component begins vesting if Coles Group achieving TSR above the 50th percentile compared to the ASX 100 Comparator Group, 100% being vested when Coles Group performs better than the 75th percentile. The TSR component of the LTI appears reasonable and meets ASA guidelines.

The company proposes to grant 223,133 performance rights to the CEO for his LTI for 2020, compared to 275,901 performance rights granted last year, calculated at the market price on the 30/6/2020 and equal to a value $3,675,000 and is 1.75 times his fixed remuneration. Whilst the number of rights issued is not as generous as last year, we still believe that an LTI of $3.675m for 2020 to be overly generous and we will monitor the performance hurdles of the LTI in future years as well as the number of rights that vest. For a company in consumer retail such as Coles Group, which operates in what is close to a duopoly market, achieving the target ROC and TSR should not be such a challenge that it justifies a large premium on the LTI compared to the norm. One could question that Coles Group is marking their executives easy in this respect for LTIs, but only time will tell. However, it is the overall package that is critical and the fact that Coles Group are willing to place more of Mr Cains remuneration package at risk is in line with ASA guidelines.

The ASA supports this resolution.