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Big changes and new challenges a year after Nine's acquisition of Fairfax

Company/ASX Code	Nine Entertainment Co. Holdings Ltd/NEC
AGM date	Tuesday 12 November 2019
Time and location	10:00 am, Ashurst Australia, 5 Martin Place, Sydney
Registry	Link Market Services
Webcast	Yes
Poll or show of hands	Poll on all items
Monitor	Don Adams assisted by Ian Anderson
Pre-AGM Meeting?	Yes, with Chair Peter Costello and Nola Hodgson, Investor Relations

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

The merger with Fairfax (FXJ), completed on 7 December 2018, changed NEC from a television broadcaster to a much larger media company with diversified interests. NEC issued 834m new shares to buy FXJ, valued at $1.383 billion, plus $57 million in cash. The number of NEC shares on issue nearly doubled to 1,705 million. The NEC shareholders now have 51% of the company and the FXJ shareholders have 49%.

The merger gave NEC the FXJ newspapers, 100% of Stan, almost 60% of Domain and a majority stake in Macquarie Media (MRN). Since then they have put the New Zealand assets of FXJ up for sale, have sold the FXJ regional and community newspapers, and acquired 100% of MRN by buying out the minority shareholders.

<u>Governance</u>

The NEC Board was restructured at the merger. David Gyngell and Janette Kendall resigned and the FXJ directors Nick Falloon, Mickie Rosen and Patrick Allaway were appointed and are standing for election at this AGM. This restructure has given NEC a Board which, apart from the CEO Hugh Marks, is equally split between old NEC and FXJ directors, and also evenly split between men and women.

An ASA focus issue this year is "skin in the game" where our standard is that directors should hold shares of a value that exceeds their annual fees after three years in position. Catherine West (40,000 shares) fails that test and Samantha Lewis (40,000 shares) and Mickie Rosen (no shares) pass at this stage since they have been directors of NEC for less than three years. Peter Costello stated that NEC policy was that directors should accumulate their share position within **five** years. Also, it has been a difficult for directors to trade shares because of blackout periods created by corporate activity.

The Board met 15 times during the year, a heavy load for directors. Ten meetings were held in the five months leading to the FXJ merger. The new combined Board met five times in the remaining seven months.

Financial performance and business conditions

The restructure of NEC due to the merger and assets sales means that the reported results are hard to compare, so NEC has provided pro-forma results which are shown in the table below. Results for the operating units show mixed results.

Television (Revenue -6%, earnings before interest tax depreciation and amortisation (EBITDA) -11%) was hurt by declining interest by advertisers as well as the switch from cricket to tennis. The audience is drifting to streaming services and advertising is moving to the internet through companies such as Facebook and Google.

Interestingly, 9Now (Revenue +51%, EBITDA +87%) did very well. 9Now has the same content as broadcast television but advertisers are attracted by “addressable advertising”. 9Now knows who is watching since viewers need to sign up to access the streaming service.

Metro Media (The Age, SMH, AFR) performed well in its digital business, and held its own on the print side. Overall it showed a 3% increase in revenue and a 65% increase in EBITDA. That’s not bad for a mature business.

Domain (revenue -6%, EBITDA -15%) held its own servicing a housing market that had collapsed in its major markets of Sydney and Melbourne. Domain aims to increase penetration in other regions through the connection with Nine television.

Stan was the star of the show. Revenues for the year were $157 million, up 62%. EBITDA was still negative at $(21) million. At the end of the year, however, revenue was running at an annual rate of over $200 million and a profitable year is expected.

At the time of the merger NEC forecast that there would be $50 million annually in cost side synergy through the merger. They claim that $22 million has been achieved by balance date, with the rest to come. Most has come out of corporate costs, but sales and IT expenses are also included. The MRN acquisition may offer further opportunity to cut such overhead costs.

NEC has a strategic emphasis on advertising sales. As well as listing the CEO and CFO as KMP, NEC also lists Michael Stephenson, Chief Sales Officer, as a KMP indicating the importance they attach to the role. In 2017, Nine television introduced 9Galaxy, an award-winning online tool for buying and selling advertising inventory. 9Galaxy has since been extended to cover 9Now advertising sales.

Summary

(As at FYE)	**2019**	**2018**	**2017**	**2016**	**2015**
NPAT ($m)	233.9	209.7	(203.4)	324.8	(592.2)
UPAT ($m)	187.1	156.7	123.6	120.3	129.5
Share price ($)	1.88	2.48	1.38	1.05	1.55
Dividend (cents)	10	10	9.5	12	9.2
TSR (%)	(19%)	87%	40%	(25%)	(26%)
EPS (cents)	13	18	14	13.5	14
CEO total remuneration, actual ($m)	4.958	5.023	2.775	1.14*	4.29

*part year

For 2019 the CEO's total actual remuneration was **56 times** the Australian Full time Adult Average Weekly Total Earnings (based on May 2019 data from the Australian Bureau of Statistics).

Pro Forma Results

(As at FYE)	**2019**	**2018**
NPAT ($m)	224.8	205.9
UPAT ($m)	198.3	170.6
EPS (cents)	11.6	10

Item 2	**Adoption of Remuneration Report**
ASA Vote	**For**

The Remuneration Report is clear and comprehensive, but we have a couple of issues as described below.

This table below shows that plan for the CEO based on his fixed remuneration of $1.4m. Short-term incentive (STI) remuneration is 100% to 150% of fixed remuneration (other key management Personnel (KMP) 50% to 75%) subject to the achievement of performance targets. It is paid 67% in cash and 33% in equity.

Long-term incentive (LTI) awards of up to 100% for the CEO and 50% for the other KMP are based on total shareholder return (TSR) and earnings per share (EPS) performance over a three-year period and are generally 100% equity. The report only comments on these targets once the award has been made since they regard the targets as commercially sensitive.

CEO rem. framework	Target* $m	% of Total	Max. Opportunity $m	% of Total
Fixed Remuneration	1.400	33%	1.400	29%
STI - Cash	0.910	21%	1.365	28%
STI - Equity	0.490	12%	0.735	15%
LTI	1.400	33%	1.400	28%
Total	4.200	100.0%	4.900	100%

The amounts in the table above are the statutory 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.

There was no increase in CEO, Hugh Marks, fixed remuneration during the year. Michel Stephenson, the Chief Sales Officer received an increase from $720,000 to $840,000 effective 1 July 2018. The CFO, Greg Barnes, received an increase from $850,000 to $900,000 on 10 December 2018. The company announced his departure on 14 August 2019. Paul Koppelman, the new CFO, joined the company on 3 September 2019. His remuneration package is yet to be advised.

Non-executive directors (NED) remuneration is clearly disclosed and seems reasonable for a company of this size and complexity. The aggregate fee pool for NEDs was set at $3 million in 2013 and has not been changed since.

Aspects of the remuneration policy of NEC that ASA takes issue with are:

1. ASA prefers that LTI is earnt over at least four, but preferably five, years. NEC LTIs vest at three years.
2. ASA prefers that at least 50% of STI be paid in equity. NEC only pays 33% of the total STI in equity.

Notwithstanding these issues the overall quality of the report is such that we will vote undirected proxies in favour. At the AGM, the ASA will advise NEC that we expect changes to remuneration structure next year.

Item 3	**Re-election of Ms Samantha Lewis as a Director**
ASA Vote	**For**

Ms Lewis was appointed to the board in March 2017 and is chair of the Audit & Risk Management Committee and a member of the People & Remuneration Committee. She is a Chartered Accountant with extensive experience including 14 years as Partner at Deloitte Touche Tohmatsu. She is on the boards of Orora Ltd and Aurizon Holdings Ltd, as well as Chair of the Audit Committee of APRA. ASA expects that Ms Lewis will soon increase her low holding of 40,000 shares.

Ms Lewis has extensive finance and accounting experience as well as experience as a director. ASA will vote undirected proxies in favour of her re-election.

Item 4	**Election of Mr Nicholas Falloon as a Director**
ASA Vote	**For**

Mr Falloon was appointed to the Board on 7 December 2018 as a result of the FXJ merger. He was Chairman of FXJ and is now Deputy Chairman of NEC. He is also the Chairman of Domain Holdings Australia. Mr Falloon has 30 years of experience in the media having been CEO at different times of both PBL and Ten Network Holdings. He holds 396,000 shares in NEC.

Mr Falloon is highly qualified, and ASA will vote undirected proxies in favour of his election.

Item 5	**Election of Ms Mickie Rosen as a Director**
ASA Vote	**For**

Ms Rosen was appointed to the FXJ Board in March 2017 and was appointed to the NEC Board following the merger on 7 December 2018. She holds an MBA from Harvard and built the foundation of her career with McKinsey & Company. She has nearly 30 years of experience in strategy, operating, advising and investment experience at the intersection of media and technology. Ms Rosen built and led businesses for brands such as Fox, Disney, Yahoo and Hulu. She was President of Tribune Interactive, the digital publishing arm of Tribune Publishing and President of the Los Angeles Times. She is currently a partner in Whisper Advisers, a boutique advisory firm based in Los Angeles.

Ms Rosen does not yet hold any shares in NEC. Due to her rich experience at a senior executive level in media and technology ASA will vote undirected proxies in favour.

Item 6	**Election of Mr Patrick Allaway as a Director**
ASA Vote	**For**

Mr Allaway was appointed to the FXJ Board in April 2016 before moving the new NEC Board on 7 December 2018 as a consequence of the merger. He has had thirty years of experience in global finance in Sydney, London, New York and Zurich. He has also had sixteen years non-executive director experience. He is a director of Domain Holdings and the Bank of Queensland, and has been a director of Macquarie Goodman, Metcash and Woolworths South Africa.

Mr Allaway holds 74,000 shares in NEC. ASA will vote undirected proxies in favour of his election due to his strong finance and directorial experience.

Item 7	**Grant of 2020 Performance Rights to CEO, Mr Hugh Marks**
ASA Vote	**For**

This is a routine motion to give effect to the company's LTI scheme. Mr Marks will receive 760,869 performance rights worth $1,400,000 at the VWAP of $1.84 around the date of the release of the FY 19 results. The rights are subject to tests for TSR and EPS growth which will determine how many of the rights, if any, will be vested in Mr Marks on 1 July 2022. ASA does not support a three-year period to determine LTI and will be looking for a longer period in next year's remuneration plan.

ASA will vote undirected proxies in favour.

Item 8	**Financial Assistance**
ASA Vote	**For**

This is another routine motion to ensure that corporate entities acquired by NEC with the purchase of Macquarie Media become part of the Common Terms Deed of the NEC group. Under this deed every corporate entity in the NEC group cross-guarantees the liabilities of the other entities in the group. If this motion were not passed NEC may have an event of default under its loan agreements. ASA will vote undirected proxies in favour.

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