Australian Shareholders' Association

Australian Shareholders' Association Limited
ABN 40 000 625 669
Suite 11, Level 22
227 Elizabeth Street, Sydney NSW 2000
PO Box A398, Sydney South NSW 1235
t (02) 9252 4244 | f (02) 9071 9877
e share@asa.asn.au

Sims knocks it out of the park in 2021-22, but yet again faces future headwinds

Company/ASX Code	Sims Limited/SGM
AGM date	Tuesday 8 November 2021
Time and location	9am AEDT he Mint, 10 Macquarie Street, Sydney, NSW
Registry	Link Market Services Limited
Type of meeting	Hybrid
Poll or show of hands	Poll on all items
Monitor	Nick Bury and Elizabeth Fish
Pre AGM Meeting?	Yes, with Chairman Geoff Brunsdon and Ann Metelo, Group Director Investor Relations

Monitor Shareholding: The individuals (or their associates) involved in the preparation of this voting intention have no shareholding in this company.

Proposed Voting Summary

No.	Resolution description	
1	Re-election of Ms Deborah O'Toole	For
2	Re-election of Mr Horoyuki Kato	For
3	Re-election of Mr Philip Bainbridge	For
4	Reinsertion of proportional takeover provisions	For
5	Remuneration Report	Against
6	Participation in LTI plan by Mr Field	Against
7	Climate Transition Plan	For

See ASA Voting guidelines and Investment Glossary for definitions.

Summary of ASA Position

Consideration of accounts and reports - No vote required

SGM's sales revenue increased 56.6% from last year to $9,264.4M and its underlying NPAT increased 103.8% to $578.9M, which basically says it all. This was a remarkable achievement against a backdrop of covid, the beginning of inflationary pressures, and generally challenging market conditions. Underlying EBIT also improved 95.6% to $756.1M.

SGM has stuck to its 5 year strategic plan which had basically begun to deliver in spades, but as electricity is such a big cost input for it, and bad energy policy both here and overseas is occasioning such stratospheric energy price rises, the market perception is that SGM's profitability will be greatly impacted going forward, as evidenced by its share price drop from about $22-50 to about $12-50 over a 3 month's time span between April and July, 2022. It has grown its core metal and cloud recycling businesses through keenly priced acquisitions, which it funded from the sale of its 50.46% interest in Sims Municipal Recycling business.

During the year SGM distributed 42.3% of its underlying profits to shareholders by paying partly franked dividends and staging an on market share buyback.

Last year the monitors wrote 'the signs are that SGM's sales revenue and profit will increase again this year, as demand in its main US and Australian markets continues to gather pace, and long suffering shareholders at least received a 72c dividend during the 2021 year. The final 30c dividend was understandably only 50% franked, given that the company derives its majority of earnings from offshore.

In fact SGM's performance during the period under review has confirmed that the abovementioned prediction was prescient, as evidenced by such a turnaround in profitability, and an increase in dividend for the full year paid from 72c in 2021 to 91c in 2022 (both dividends paid having been partly franked).

However, no matter how well SGM runs its business, increasing inflation, an anticipated business downturn occasioned by a likely recession to come, and huge likely electricity price hikes going forward are likely to dampen its immediate performance outlook.

SGM, whose fortune is tied to commodity cycles, will always go up and down with bull and bear commodity markets to some degree, but it's making a great fist of its long term strategic plan, and maximises its returns by making the best of whatever circumstances in which it finds itself placed

Summary

(As at FYE)	**2022**	**2021**	**2020**	**2019**	**2018**
NPAT ($m)	578.9	284.1	-58.1	72.3	191.2
EBIT ($m)	756.1	386.6	-57.9	230	279
Share price ($)	13.89	14.39	10.58	11.04	16.39
Dividend (cents)	91c	72c	6c	53c	53c
Simple TSR (%)	-2%	42.01%	-10.81%	-31.60%	16.24%
Statutory EPS (cents)	303.1c	112.8c	(131.2c)	74.2c	101.1
CEO total remuneration, actual ($m)	$8.56	$4.73	$6.46	$5.14	$5.74

Simple TSR is calculated by dividing (change in share price plus dividend paid during the year, excluding franking by the share price at the start of the year.

Election or re-election of directors

Ms Deborah O'Toole has been an SGM NED for the past 8 years and is an experienced director. Her other current directorships are as the Chair of Transurban Queensland, as an NED of Pacific National Rail Group, of Credit Union Australia, Alumina limited and Sydney Airport Corporation Limited. Her services seem to be in high demand, but she will be asked about how much spare time she has to devote herself to her SGM NED duties. Her previous commercial experience had is relevant to her SGM duties.

Her executive experience has been in the mining and transport and logistics industries, in management, operations and finance sector roles. More specifically, she has been the CFO of MIM Holdings Limited, Queensland Cotton Holdings Limited and Aurizon Holdings Limited. Her previous board experience includes directorships of the CSIRO, Norfolk Group, companies within the MIM and Aurizon Groups, and Government and private sector boards, and acting as Chairperson of the Audit Committees of CSIRO, Norfolk Group and Pacific Aluminium.

There will soon come a time when due to the length of her NED tenure she would no longer be able to be considered as an independent director.

Mr Kato was appointed as an SGM director in November 2018. Mitsui & Co hold a 16.5% interest in SGM and are entitled to appoint a representative to SGM's board.

Mr Kato has longstanding experience working in the mining and oil industries and brings 'growth strategy' expertise to the board. He is a member of the Audit and Safety, Health, Environment, Community & Sustainability Committees. He commenced his business career working in Mitsui's iron ore division, where he gained his mining industry experience. He has held various positions in Mitsui's oil and gas divisions during his long career with that company. ASA believes that assumedly Mitsui knows who amongst their employees can best represent their interests on SGM's board. As Mitsui is a fellow traveller with other SGM shareholders similarly seeking for SGM to corporately perform as well as possible, ASA is in favour of Mr Kato's re-election.

Mr Bainbridge's senior executive experience is primarily in the oil and gas sector across exploration, development and production. He has worked in North America, Europe, Asia and Australia. He was the executive general manager for Oil Search limited and he has worked at Pacific National and BT Group. He is currently an independent director of Beach Energy Ltd and Newcrest Mining, and chairman of the Global Carbon Capture and Storage. His appointment will not be opposed, but he will be asked about what relevant experience he has that relates to the scrap metals trade and to SGM's worldwide operations.

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

The remuneration report is extensive but easy to understand. The remuneration committee have indicated some changes will be made to its structure in FY23. These are covered in the section headed "Looking Ahead to Fy23". There are all the regular remuneration components of STI, LTI and Fixed in this report.

For STI 80% relates to company performance using one financial measure, being underlying EBIT. 50% of STI is awarded at threshold and 100% at budget/target, and where underlying EBIT reaches maximum an additional 100% is payable. Neither budgets or targets or threshold for vesting are disclosed. Fy22's Underlying EBIT at $756.1m was significantly above budget. KMP achieved STI of 98% to 100% of budget, and 160% of maximum target was achieved.

The remaining 20% relates to individual performance goals (IPGs) that are set in a number of key areas that focus on safety and business transformation, ERP, culture, leadership and people, as well as optimisation. The Board assesses the IPG achievement, and executives can earn a maximum of 120% achievement for the IPG component of the STI. Details of executives achievements against goals are shown at section 2.6 (page 72). The section does not show how well each of the executives or the CEO met their respective goals, although we note that 120% of the 20% was achieved. The goals that are shown in the Remuneration Report are very much what any investor would be expecting an executive to do as part of their job. The measures do not offer quantifiable performance metrics to support the award decisions. The STI awarded is paid in cash in the month of September following release of audited results. The Board retains discretion to adjust STI awards as warranted.

ASA does not support all STI being paid in cash and believes that there should be an equity component. The ASA put this view to the Chair of the Rem Committee in FY21 and she said Sims would retain these cash payments due to SGM's volatility of earnings.

The LTI component

22% TSR Rights incentivise achievement of higher shareholder returns relative to peer companies in the ASX 200 materials and energy sectors, over the three-year performance period of 1 July 2021 through to 30 June 2024. Rights vest after three years, with the quantum subject to attainment of the performance conditions, which is performance measured against a peer group. The comparator group used to measure TSR performance are those constituent companies listed as of 1 July 2022 in the ASX 200 materials and energy sectors. TSR must be 50% or higher than that of the comparison group for the LTI's to vest. 50% of Rights vest at the 50%, then 100% vest at the 75% level.

45% Strategic Rights incentivise achievement of the Company's strategic goals over the three-year performance period of 1 July 2021 through 30 June 2024 using a ROC performance metric. Rights vest after three years, with the quantum subject to attainment of the performance conditions, and potentially further modified for the Company's return on capital (ROIC) performance. Underlying not statutory EBIT is used in the ROC calculation. 70% of Rights vest when a ROIC of 10% is reached, then on a straight line basis where 100% is awarded when 12% is reached. It does appear that even where ROC is < 10%, 70% of strategic rights still vest, see P66 of SGM's annual report (AR).

33% SSI Rights incentivise achievement of the Company's strategic goals over a one-year performance period of 1 July 2021 through 30 June 2022, and the subsequent share price performance over the next three to four years after vesting.

Earned SSI Rights vest (subject to escrow requirements) after one year, with the quantum subject to attainment of a number of near term objectives directly aligned to the businesses long-term global strategies. It is paid in the form of a cash award. The SSI cash award is used to purchase deferred shares at on-market price (after withholding of any required taxes). The resulting deferred shares are subject to holding periods of three and four years, (50% for each year). Dividends are earned during the holding period. SSI rights weightings and outcomes are shown on p74 of the AR. The measures seems to be in line with expectations, however some of the criteria may also be covered in the STI criteria. There are 6 strategies in all. We still do not see quantifiable performance metrics although the ASA understands the Board will be introducing individual weightings of goals for the FY23 Grants in response to stakeholder feedback. The Remuneration Chair has said these rights avoid the tax event, allowing executives to build up skin in the game.

Until FY22, the number of TSR Rights granted is determined based on the fair value of the rights at the time of approval by the Board. The fair value is calculated using the Monti Carlo simulation option pricing model. The ASA notes that from FY23 allocation of rights will be based on a face value methodology.

ASA does not support the STI being paid fully cash, or cash awards for LTI measures, and three years is insufficient time for LTI projects to be effective. The single year period for measuring SSI, is not long term. Underlying EBIT should not be used to calculate awards. There is a lack of clarity on KMPs targets. The ASA considers that although some improvements will be made to the remuneration practices in FY23, we would not vote undirected proxies in favour of the resolution.

The annual performance based long-term incentive plan (LTIP) award is equal to 200% of the CEO's fixed remuneration and has a value of $3,428,840. The ASA will vote undirected proxies against the resolution seeking shareholder approval for the proposed grant of performance rights to the CEO and Managing Director Mr Alistair Field, under the company's Long Term Incentive Plan.

Reinsertion of proportional takeover provisions

We prefer full takeovers so that shareholders are not left with a controlling shareholder and usually support these resolutions.

Appendix 1
Remuneration framework detail

CEO rem. Framework for FY22	Target* $m	% of Total	Max. Opportunity $m	% of Total
Fixed Remuneration	1.716	25%	1.716	21%
STI – Cash	1.716	25%	3.105	38%
STI – Equity LTI	- 3.432	- 50%	- 3.350	- 41%
Total	6.864	100%	8.171	100%

The amounts in the table above are the amounts that are envisaged in the design of the remuneration plan.