



Milton merger propels Soul Patts into the top 50

Company/ASX Code	Washington H. Soul Pattinson and Company Limited / SOL
AGM date	Friday 9 December 2022
Time and location	12.00 noon at the Wesley Conference Centre, 220 Pitt Street, Sydney
Registry	Computershare
Type of meeting	Physical and webcast (watch only – no questions or voting)
Poll or show of hands	Poll on all items
Monitor	Peter Gregory assisted by Norman Windell
Pre AGM Meeting?	Yes with Chair Robert Millner

Monitor Shareholding: The individuals involved in the preparation of this voting intention have a shareholding in this company.

AGM webcast

Washington H. Soul Pattinson (WHSP) are returning to a face-to-face AGM in Sydney. This year there won't be displays by WHSP investee companies prior to the AGM. The AGM, while it will be webcast, it won't be interactive. Shareholders who can't attend will need to vote (or appoint a proxy) and submit written questions by 12 noon on 7 December 2022 as described in the Notice of Meeting.

Summary of issues for meeting

Board renewal, director independence, and key person vulnerability

The WHSP board comprises 7 directors – 5 are seen as independent. Robert Millner and Thomas Millner are not independent. Robert Millner has been a director for 38 years and chair for 23 years; he is a substantial WHSP shareholder and is chair of Brickworks which is also a substantial WHSP shareholder. Thomas Millner has served as a WHSP director for 11 years and is a substantial WHSP shareholder.

ASA recognises, that while this is an unusual situation for a large ASX company, WHSP, under this board and management, continues to deliver favourable outcomes for all shareholders.

The annual report on p29 discusses the topic of director independence, the action taken, including the appointment of Michael Hawker as Lead Independent Director and a clear conflict of interest policy to ensure the company is operating in the best interests of all shareholders. It includes a statement of support for Robert Millner as chair.

Nevertheless, in representing the many individual shareholders of WHSP, ASA has some concerns:

- WHSP publishes a minimal board skills matrix, and it appears that the independent directors are well qualified. However, to enable shareholders to make more informed decisions when voting for directors we ask that the board skills matrix be expanded to show the skills, together with the level of competence/ experience, of each director.

- WHSP has a Nominations Committee that is responsible for board renewal and oversight of the defined selection process. This includes compilation of a short list by an external recruitment consultant based on the required target profile. What happens after the short listing and what is the involvement of independent and non-independent directors in this process?
- From reading the summary of each director there appears to be a bias towards finance related backgrounds. WHSP, as an investor, has a very diverse portfolio of assets and would benefit from a broadening their range of skills and experiences to draw upon in board deliberations. Other ASX companies, with a narrower business focus, but of a similar size to WHSP have boards with a larger number of independent directors.
- Michael Hawker, the lead independent director has now been on the board 10 years. While WHSP does not have a formal tenure policy, ASA will no longer regard him as independent if his term as a director exceeds 12 years.
- It is common practice for WHSP to have board representation on its strategic investments. While this is supported it raises a concern that this responsibility largely rests with Robert Millner. With the quality of WHSP directors, and with a likely expansion of strategic investments it appears that other directors are an underutilized resource in the important oversight of that portfolio.
- The board has policy for an annual board evaluation and in FY22 this was conducted by an external facilitator. Were there any recommendations from this evaluation, especially reading points listed above?

Robert Millner, over his years as a director, has had a very significant involvement in the direction of WHSP and has been instrumental in working with, and on the board of companies in the strategic investment portfolio. (Including some, such as New Hope and TPG, from the very early days of these businesses.). He continues to be actively involved with, has a close association with and believes he makes a significant contribution to the successful operation of those strategic investment companies.

Under his leadership WHSP during the past 20 years has seen an annualised TSR of 12.2% compared to 8.8% for the All-Ordinaries Accumulation Index and market cap grow from \$700 million to \$10 billion. He is a very experienced and competent director who has a strong grasp on the issues for each of the strategic investee companies and WHSP.

As a non-executive director, he has a greater involvement in WHSP than would be expected. He and Todd Barlow together are crucial to the success of WHSP, and it appears that the company is exposed to a material risk of loss of either of these two people. This vulnerability was discussed during the pre-AGM meeting. Millner responded that the company had good people and has a succession plan in place. However, it is probable that a departure of either would result in a period of disruption to the company, and that it may be challenging for whoever were to follow on to become quickly effective. We will ask about mitigation strategy at the AGM.

Note it is only Warwick Negus that has had similar sized ASX chairmanship experience (and that is only since Feb 21) on the board.

Evolving strategy and reporting structure

WHSP is an active manager of its investment portfolio, and FY22 saw significant changes as described in Key events. Also, WHSP took advantage of high equity prices to sell equity and other

assets yielding a working capital increase during the year of \$735 million and is reporting net working capital of \$274 million.

With this access to liquidity there are plans to expand exposure to:

- private equity opportunities that will provide platforms for future growth;
- early stage and high growth companies (through direct investment and convertible notes) as valuations for appropriate assets become more reasonable;
- and to leverage existing relationships and expertise into a growing lending market, especially in market segments vacated by the major banks.

This is a reflection of a company that is agile and responsive to opportunities, while also taking a long-term perspective of value.

This refocus has meant an adjustment in how WHSP is reporting its portfolio and readers are encouraged to read the Portfolio Review section (p14-19) of the Annual Report to gain a better understanding of how WHSP are adapting to opportunities.

It would be useful, in addition, for shareholders to see the portfolio (excluding large cap) mix by sectors – as a suggestion these may be Agriculture, Resources; Technology and Communications; Healthcare; Financial; Other Industrials and Property.

Proposed Voting Summary

No.	Resolution description	
2	Adoption of Remuneration Report for year ended 31 July 2022	For
3a	Election of Ms Joe Pollard as a Director	For
3b	Re- election of Mr Robert Millner as a Director	For
4	Grant of Performance Rights to the Managing Director	For

See [ASA Voting guidelines](#) and [Investment Glossary](#) for definitions.

Summary of ASA Position

Consideration of accounts and reports - No vote required

Financial performance

WHSP posted a statutory NPAT loss of \$12.9 million mainly due to a one off, non-cash goodwill impairment of \$984.6 million arising from the Milton acquisition.

WHSP operate their business and internally report using “Alternative Performance Measures” that are more reflective, given the various ownership structures of WHSP investments, of outcomes for shareholders. These are described on p21 of the annual report and are reconciled to statutory measures. These are:

- Group Regular NPAT - for FY22 this was \$834 million, up 154% from FY21. This measure excludes non-regular items of income and expense which by nature are outside the ordinary course of business or are part of ordinary activities but are unusual due to their size. At the pre-AGM meeting, the chair described the methodology that is consistently

applied to determine regular profit. This measure is seen to be a valid indicator of the ongoing business performance.

- Pre-tax Net Asset Value – in FY22 this was \$9.96 billion having increased 72% on the prior year. A major influence on this was the merger with Milton that increased the NAV by \$3.8 billion. To exclude the effect of Milton consider that for the NAV per share WHSP exceeded the All Ordinaries Index by 20.2%. This index decreased by 6.4% over the same period. This measure reflects the underlying value of WHSP to investors and is expected to be a share price driver.
- Net Cash Flow from Investments is a measure that excludes non regular cash inflows and outflows to demonstrate the underlying cash flow generated by the investment portfolio. In FY22 this was \$348 million up 93% on the prior year. The board takes this into account in determining dividends.

As an Investment House that may be compared to managed funds or ETFs an important comparator is the management cost of investment activities. While WHSP does not publish an exact number, they indicate around 0.2% of NAV.

Governance and culture

WHSP is a unique company on the ASX – following the Milton merger WHSP now has a market capitalisation of around \$10 billion making it in the top 50 ASX listed companies. But it only has a direct staff of 47 people. This enables a good relationship between the board, management and staff. Specifically, key management are invited to attend board and committee meetings; Other members of management and staff regularly attend and present to the board on matters as subject matter experts; Further information is provided on request, in response to board questions and particular areas staff have interest and oversight responsibility; And informal meetings between the board, management and staff occur from time to time.

WHSP has a risk plan that describes the process used to identify and manage risk, but provides limited information as to what the risks and mitigation strategies are.

The Sustainability Report recognises that successful long-term investing is sustainable investing. It describes the actions being taken within WHSP within its direct operation. It also describes the manner in which WHSP considers ESG in its investment screening process and how it seeks to influence companies it invests in.

At previous AGMs activist investors have disrupted the AGM with questions and comments about New Hope. From a review of the New Hope annual report it can be seen that the company, with scope 1 and 2 emissions is working hard to minimise these in its operation and through efforts to rehabilitate land no longer being mined and to responsibly manage its use of water is minimising its effect on the environment. As a miner of relatively clean coal New Hope is enabling operators of coal fired power stations to keep their emissions down.

WHSP employs 47 people in its head office. The board of 7 people has 42% female, executive and senior management is 8% female, and other staff is 60% female. WHSP recognises that diverse perspectives and challenging opinions is integral to good investment outcomes and has expressed a commitment to diversity and the inclusion of diversity criteria into people related processes.

Key events

On 5 October 2021, the merger with Milton was completed, increasing the NAV of WHSP by \$3,844 million, largely in the Large Caps Portfolio. Five Milton people joined WHSP including the

CEO Brendan O’Dea who became WHSP’s Chief Investment Officer. This script for script merger doubled the number of WHSP shareholders and increased the WHSP market cap to \$10.8 billion. Watch the [Milton merger video](#) for more information.

In December 2021, WHSP completed the sale of its investment in Australian Pharmaceutical Industries Limited to Wesfarmers for \$131.2 million, with a subsequent payment of \$16.2 million received in March 2022.

In May 2022, WHSP purchased the 57% it did not own in Ampcontrol Limited for \$99.7 million. Ampcontrol remains in the Private Equity Portfolio for reporting.

In July 2022, WHSP completed the sale of its investment in Round Oak Minerals Pty Limited in exchange for cash and a 30.2% stake in Aeris Resources Limited valued at \$98 million. In the prior year Round Oak was included in the Private Equity Portfolio. The investment in Aeris is now included in the Strategic Portfolio

WHSP held [Investor Briefing Meetings](#) in Sydney, Melbourne and Adelaide to enable shareholders to meet with management, see the WHSP long term track record and gain some valuable insight into WHSP’s investment strategy now and for the future.

Summary

(As at FYE)	2022	2021	2020	2019	2018
NPAT (\$m)	-12.9	273.2	953	248	266.9
Regular profit after tax (\$m)	834.6	328.1	169.8	307.2	331.1
Share price (\$)	25.7	35.82	20.93	20.89	21.82
Dividend (cents)	72	62	60	58	56
Simple TSR (%)	-26	74	3	-2	
EPS (cents)	4	114	398	104	
CEO total remuneration, actual (\$m)	\$3.5	\$2.9			

CEO’s total actual remuneration compared to annualised Australian Full time Adult Average Weekly Total Earnings (based on data from the Australian Bureau of Statistics is 36.8X <http://www.abs.gov.au/ausstats/abs@.nsf/mf/6302.0>).

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 and re-election of directors

Ms Pollard is an experienced executive and director. Her sales, marketing, media and digital technology skills and previous senior roles at Telstra, Nike and Ninemsn in Australia and overseas

will add to the overall board skills and will enable her to make a valuable contribution to the board. She joined the board of WHSP in March 2022 and we will vote for her election.

With Mr R Millner, his length of service as a director, and non-independent status as chair deviates from ASA guidelines. The situation with the board and his role on it has been discussed earlier. The question of ASA supporting his re-election was discussed during the pre-AGM meeting.

In determining how to vote on this item the overriding consideration is what is the best outcome for shareholders. Offsetting the risks associated with a long standing, non-independent director is the loss of an experienced director who is making a major contribution to WHSP.

Therefore, we will vote undirected proxies for his re-election.

But, at the AGM ASA will raise concerns about the key person vulnerability that WHSP is exposed to and seek effective mitigation.

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

The Remuneration Report is largely in line with ASA Guidelines. Importantly there is a good connection with shareholder interests, and it is positive to see all WHSP staff being invited to participate in the LTI.

There are some changes we would like to see made and questions that we will seek responses to at the AGM:

- Given the size of WHSP the use of ASX 200 and All Ordinaries indexes no longer seem appropriate, and we request the use of other benchmarks that are better aligned to WHSP.
- With relative TSR it is more common practice to compare to a set basket of companies and to match against a particular percentile point.
- ASA discourages the use of retesting provisions in LTIs. An extension of time to achieve the set metric rarely delivers an outcome and from a motivation perspective it is better to simply move onto the next period.

The WHSP Remuneration Report is aligned with shareholder outcomes and undirected proxies will be voted for.

CEO grant of Performance Rights

The resolution for the grant of Performance Rights for the CEO is for 129,765 rights. The number of rights is determined by dividing the CEO's maximum \$ LTI allocation by the volume weighted average share price as described in the notice of meeting. The hurdles are described under LTI in the Appendix. This is a key part of the remuneration plan and undirected proxies will be voted for.

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Appendix 1

Remuneration framework detail

STI

The STI has a financial hurdle of 50% regular cash to the parent company (from which dividends are funded) being more than the prior year and 50% net asset value after tax (driving share price growth) being greater than the ASX200 Accumulation Index. If these hurdles are both met (i.e. threshold is achieved) the size of the STI pool is determined by the amount above the threshold. For regular cash to the parent company the maximum is at 9% above the prior year and for NAV per share at 7% above the ASX200 accumulation index.

Once the STI pool is established the amount that is paid is determined based on both financial and non-financial performance measures. These are established at the start of the year based with equal weighting across these categories:

- Investment Management
- Company Management and advice to the Board
- Interaction with the Investment Community
- Risk Management

In FY22 the CEO was awarded 100.8% of his pro rata entitlement to the STI pool.

The CEO holds 210,066 valued at approx. \$5.8 million and has 241,079 share rights subject to performance conditions which if vested at today's price would be worth approx. \$6.7 million. He has skin in the game, so the STI is paid in cash to reduce the need to sell shares to meet tax obligations from LTI vesting.

LTI

The LTI award of Performance Rights is based on the achievement of two separate metrics:

- Tranche 1 of 50% - WHSP TSR compared to the All Ordinaries Accumulation Index with maximum awarded at the index plus 3% CAGR.
- Tranche 2 of 50% - CAGR in NAV per share with the maximum awarded at exceeding 10% CAGR.

For more details refer to p62-3 of the Annual Report.

When the vesting conditions are satisfied the value of the rights will be evaluated and a decision made as to whether the payment is in shares or cash.

The LTI metrics are measured over 3 years. There is a provision for retesting by extending the measurement period for one year in vesting has not occurred. This would mean a very high bar for any meaningful reward. To date retesting has not delivered any benefit.

Following the Milton acquisition all staff have been invited to participate in the LTI.

CEO rem. Framework for FY22	Threshold \$m	% of Total	Target* \$m	% of Total	Max. Opportunity \$m	% of Total
Fixed Remuneration	1.51	67%	1.51	53%	1.51	40%
STI - Cash	0.60	27%	0.75	27%	1.13	30%
STI - Equity	0	0	0	0	0	0
LTI	0.14	6%	0.57	20%	1.13	30%
Total	2.25	100%	2.83	100%	3.77	100%

For FY22 the CEO received:

- Fixed remuneration \$1,555,615
- STI \$0 – FY21 financial hurdles were not met
- LTI \$1,982,661 rights vested
- Total WHSP \$3,538,276
- New Hope director fees \$143,054
- Consolidated entity total \$3,681,330

The CEO's total remuneration for a \$10 billion market cap company is seen to be low.