Australian Shareholders' Association

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Corporate hero of the pandemic?

Company/ASX Code	Woolworths Group Limited / WOW
AGM date	Thursday 12th November 2020
Time and location	10:00 am, virtual meeting only.
Registry	Link Market Services Limited
Webcast	Yes, link at https://agmlive.link/agm/wow20/register
Poll or show of hands	Poll
Monitor	Don Adams assisted by Julieanne Mills
Pre-AGM Meeting?	Yes, with Chair Gordon Cairns; Holly Kramer, Independent Non-Executive Director, Chair of People Performance Committee; Marcin Firek, Company Secretary; Paul van Meurs, Head of Investor Relations

NOTE: ASA WILL BE ATTENDING THE VIRTUAL MEETING VOTING THE PROXIES WE RECEIVE AND ASKING QUESTIONS, AS NORMAL

The individuals (or their associates) involved in the preparation of this voting intention have a shareholding in this company.

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

2020 was a dramatic year for Woolworths (WOW). Not least was the role they played in keeping supply lines working during the COVID-19 pandemic. They also had to deal with the drought and with keeping stores stocked in bushfire isolated communities. They appear to have finally handled the underpayment issue which caused such problems last year.

Revenue

Woolworths' revenue increased in 2020 to $63.7bn, up 8.1% from 2019 normalised for discontinued operations and the 53-week year. This strong growth came from all business units except Hotels, which were affected by pandemic shutdowns.

Australian Food was up 8.3% normalised to $42.2bn (Coles was up 6.8% to $33 bn), powered by the pandemic with both panic buying and consumers eating at home more often. Revenue was up 6.4% in the first half of the financial year, but growth increased to 10.5% in the pandemic affected second half. However, 4Q costs also increased due to safety protocols put in place for COVID-19.

Woolworths has the largest share of the Australian grocery market at about 33% but they feel that during the pandemic they may have lost share to independents since customers liked to shop closer to home. There was an interesting swing in behaviour in Q4 2020 when customer visits to stores fell by 11% but the number of items per basket increased by 15.4%.

Woolies X, online food sales were up 43% to $2bn, 69% in Q4. WOW had to invest in more facilities and people to support this pandemic related growth.

New Zealand Food increased revenue by 10.5% normalised to AUD$6.8bn presumably also due to the pandemic.

Big W was up 10.5% with sales of $4.1bn. For the first time this division showed positive EBIT of $39m. While this was helped by pandemic sales, WOW maintains that Big W was on track to profitability in 2020 prior to the pandemic.

Endeavour Drinks was also up 9.9% to $9.3bn revenue. With bars and hotels closed more people were drinking at home.

Hotels were down 19.5% to $1.32bn due to pandemic closures. At the time of writing (Oct 2020) 85 hotels are closed in Victoria alone, so this problem continues. Nevertheless, Hotels were profitable contributing EBIT of $172m.

Strategic Initiatives

During 2020 WOW completed the restructuring of the Endeavour Group (Drinks and ALH Hotels) to the point where it is ready to be divested as a separate company. The actual divestment is deferred until 2021. They also announced an investment exceeding $700m in the NSW supply chain, building two new automated distribution centres and closing three existing facilities.

After year end, in August 2020, WOW announced a major investment in PFD Food Services, a major player in the business-to-business market. WOW will pay $552m for a 65% equity stake and for 26 freehold properties. ACCC approval is being sought for this deal.

Effect of the COVID-19 pandemic

While the pandemic affected revenue there were other issues for WOW. Pandemic costs in 2H 20 amounted to $404m including spending of $105m on cleaning and PPE, $54m on contractors and security, $117m on additional staff costs. Staff (team members as WOW likes to call them) increased by about 20,000 to over 200,000 in total as WOW absorbed some of the March job losses.

WOW received no government benefits such as Jobseeker, and they have decided not to take up the new Jobmaker program since they would rather give extra hours to their existing part-time staff.

The company is proud of the way the staff responded to the requirements of the pandemic, with a noticeable drop in absenteeism. As a reward they created the “Better Together” program which we describe below under remuneration.

Governance, culture and sustainability

This year has shown how important governance and culture are to a company’s success in crisis management. The Board and the CEO Brad Banducci have managed this crisis well, they have lead the way, prioritising safety, adapting to the rapid shift to online sales and pick up arrangements, prioritising the disadvantaged and managing the chaos that ensued with COVID shutdowns, on top of the earlier bush fires and an ongoing drought.

Woolworths has an impressive sustainability and ESG policy, based around the United Nations Global Compact and it is making good progress. Goals are defined and plans to achieve them are in place and measured. The 78-page Sustainability Report is comprehensive covering a broad range of areas including embracing diversity and gender equality, the reduction of emissions and waste, and responsible sourcing. WOW is also identifying and managing risks associated with climate change through the Task Force on Climate-related Disclosures. It has committed to zero emissions by 2050.

What is impressive is that by embedding the values into the business whether its employing refugees in the areas in which they live, or installing solar panels on its distribution centres, or investing in organic farms, it makes sense for the business as well as being good for society as a whole.

It is also admirable that the company is committed to donating 1% of EBIT to its partner organisations, including the Salvation Army, Rural Aid, Foodbank, and Lifeline.

Board

The Board of Woolworths is well equipped with the skills and experience to run one of Australia's largest businesses. The Skills Matrix is impressive with all but one of the identified skill sets being achieved by at least 8 out of 9 directors. The Board is 56% female but WOW's gender diversity target of 40% for senior executives and management is not met with only 35% of these positions held by women.

Jillian Broadbent retires from the Board at the AGM after 9 years. Maxine Brenner will join the board on 1 December 2020 and will stand for election at the 2021 AGM. The board will therefore maintain 56% of female directors.

Senior management changes

Claire Peters is to move from managing director Woolworths Supermarkets, to managing director B2B and Everyday Needs. Natalie Davis the current manager Woolworths NZ, is to return to Australia to become managing director of Woolworths Supermarkets. Colin Storrie will take up the role of managing director new business and partnerships. WOW has also appointed a chief medical officer to help with COVID health and safety, and David Walker has been appointed chief risk officer moving from the CEO of Big W. He will be replaced at Big W by Pejman Okhovet, a new hire to the WOW group.

Profit

EBIT in 2020 was basically equal to 2019 normalised at $3.2bn. Net Profit After Tax was down 57% principally due to significant items after tax of $437m. This includes after tax costs of $123m for the NSW supply chain reorganisation, $185m for Endeavour Group transformation costs, and $129m in costs for remediation of the salaried team member underpayments (see remuneration section).

Summary

(As at FYE)	**2020**	**2019**	**2018**	**2017**	**2016**
NPAT ($m)	1165	2692	1724	1534	(1235)
UPAT ($m)	1602	1751	1605	1422	1476
Closing Share price ($)*	37.28	33.23	30.52	25.54	20.89
Dividend (cents)	94	102	103	84	77
TSR (%)	15.3	12.3	23.1	25.5	(18.2)
EPS (cents	93	206	133	119	(98)
CEO total remuneration, actual ($m)	9.45	12.60	3.87	4.47	2.18

For 2020, the CEO's total actual remuneration was **103 times** the Australian Full time Adult Average Weekly Total Earnings (based on May 2020 data from the Australian Bureau of Statistics).

Item 2	**Re-election of Scott Perkins as a Director**
ASA Vote	**For**

Scott Perkins was appointed to the board in September 2014. He has extensive experience in strategy, mergers and acquisitions and capital markets. His executive career in investment banking includes the role of senior executive at Deutsche Bank from 1999 -2013. Scott has been a director of Origin and Brambles since 2015 and has just been appointed chairman at Origin. He is chairman of the Audit and Risk Committee and is a member of the People, Performance and Nominations Committees. The chairman spoke of Mr Perkins passion for ESG, as retiring chair of the Sustainability committee, his very strong contribution to the board and the value of his expertise for WOW's disposals and acquisitions.

Mr Perkins has 17,473 WOW shares well past his director shareholding requirement.

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

Underpayment of salaried staff

Last year WOW announced a serious underpayment of managerial staff on salaries who would have been entitled award rates if that would have made them better off. The costs were then estimated at $200-300m.

As at the end of the 2020 financial year WOW has recognised total costs of $500m. This is made up of $390m in back pay, plus $110m in interest and other costs. Total cash payments of $258m have been made by July 2020 and the program continues. It is taking time to resolve since there is a vast amount of data to be processed to measure the shortfalls.

The costs have been accounted for as follows under AASB 108:

1. $263m has been written off against profit in years up to 2018, by reducing 2018 retained earnings. WOW reviewed the prior year STI and LTI payments and determined that the effect would not have been material.
2. $52m was expensed against 2019 profit. Since they had made a provision of $50m for that year the net effect was to reduce EBIT by $2m and NPAT by $1m.
3. A provision of $185m before tax was taken in 2020. New problems had been discovered in other entities such as Dan Murphy's.

WOW identified the cause of the problem as "multiple points of system failure". Consequences have been that the chair, Gordon Cairns, has forfeited 20% of his board fees, the CEO and chief people officer have voluntarily given up their 2020 STI and the group executive committee received a 10% reduction in their STI to 70% of target.

Better together award

In recognition of the contribution of staff during the pandemic 106,000 permanent team members not eligible for STI were each given $750 in WOW shares and $250 WOW gift cards. Another 53,000 casual workers were given $100 gift cards. This program was funded to $67m by the company with the rest coming from a reduction in STI awards from 104% to 80% of fixed remuneration (90% in New Zealand).

Remuneration structure

STIs are paid 50% in cash and 50% in two-year deferred equity. It depends on five quantified targets: sales, EBIT, inventory, customer satisfaction, and safety. The EBIT target was missed in 2020 and customer satisfaction barely reached entry level. But the other three exceeded stretch targets, particularly team member safety which had been a focus issue. The result was an award level of 104% of target, this was reduced to 80% by the board (90% in New Zealand) and the proceeds of the reduction applied to the "Better Together" program.

LTIs are paid in three-year share rights and the percentage vested will depend on three targets: relative TSR, sales per square metre, and return on funds employed (ROFE). The 2018 award vested at the end of 2020, the profit entry level was not achieved, but relative TSR at 86th percentile was close to the stretch target of the 90th percentile. Sales/m^2 exceeded the stretch target, and the consequent award was 128.6% of target.

For the CEO this amounted to 64.3% of the share rights awarded to him in 2018. The number of vested shares were grossed up for the dividends that would have been paid on them and with share price appreciation since 2018 the actual value of his LTI was $5.1m. This, along with $2.6m base salary and $1.7m deferred STI equity, gave him total actual remuneration for 2020 of $9.4 m.

The WOW remuneration policy has a lot to commend it with definite targets, 50% equity in STI, malus provisions, and non-financial targets. We will vote in favour of the remuneration report, even though the ASA prefers a four to five year vesting for LTIs rather than the three years used by WOW.

CEO rem. Framework for FY 20	Target* $m	% of Total	Max. Opportunity $m	% of Total
Total Fixed Remuneration	2.60	33.33%	2.60	23.80%
STI - Cash	1.30	16.67%	1.95	17.85%
STI - Equity	1.30	16.67%	1.95	17.85%
LTI	2.60	33.33%	4.42	40.47%
Total	7.80	100.0%	10.92	100%

The amounts in the table above are the 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.

Item 4	**Approval of F21 LTI grant to CEO Brad Banducci**
ASA Vote	**For**

The grant of 120,557 share rights to Mr Banducci is somewhat lower than in previous years for two reasons. First, the share price is now higher and secondly, the maximum to be vested is 170% of fixed remuneration compared with 200% in earlier years.

Corporations Law requires a vote on this motion because Mr Banducci is a director of WOW. Since we approve the remuneration policy, we will vote for this motion.

Item 5	**Renew approval of termination benefits for three years**
ASA Vote	**For**

Under the Corporations Law shareholder approval is required for managerial or executive termination payments. ASA policy generally opposes the granting of termination benefits that would exceed one-year fixed remuneration. In this resolution WOW is seeking to extend an approval granted in 2017 which gives the board discretion in determining how much of the unvested equity component of STIs and LTIs will vest. Since the Notice of Meeting has a detailed explanation of the policies the Board would follow under different circumstances, and since these policies seem reasonable, the ASA will support the resolution.