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

Quarter of a billion dollar impairment torpedoes profit

Company/ASX Code	ALS Limited/ALQ
AGM time and date	10am AEST on Wednesday, 31 July 2024
Location	The Westin, 111 Mary Street, Brisbane
Registry	Boardroom
Type of meeting	Hybrid
Monitor	Paul Donohue
Pre-AGM Meeting	Yes, with ALS Global Chair, Bruce Phillips

Monitor Shareholding: The individual involved in the preparation of this voting intention has no shareholding in this company.

1. How we intend to vote

No.	**Resolution description**	
2	To elect Erica Mann as a Director	For
3	Adoption of the Remuneration Report	For
4	Increase in fee pool for non-executive Directors	For
5	Grant of 2024 Performance Rights to Malcolm Deane	For
6	Contingent business – Conditional resolution to hold a Spill Meeting	Against

2. Summary of Issues and Voting Intentions for AGM/EGM

- Last year's first strike on remuneration, and potential for a second.
- Impairment on the Nuvisan investment

See ASA Voting guidelines and Investment Glossary for definitions.

3. Matters Considered

About ALS Global

ALS provides testing, inspection and certification (TIC) services. This involves testing the purity of air, water, food, minerals and pharmaceuticals and inspecting / certifying sites and equipment.

They operate from 430+ locations in 70+ countries and employ more than 20,000 staff worldwide. Global operations are headquartered in Houston, Texas with the corporate HQ in Brisbane.

The company can trace its heritage back to "Campbell Brothers", a Brisbane based soap manufacturer founded in 1863 and publicly listed in 1952.

ALS is organised into two divisions. Life Sciences with two business streams of Food & Pharmaceutical and Environmental. Commodities encompassing Minerals and Industrial Materials. Each of these business streams is responsible for its own profit and loss. The business steams are supported by shared services.

Accounts and reports

ALS's underlying operating results were a bit softer than last year. Underlying revenue of $2.586b was up 6.8% but underlying earnings (EBIT) only nudged up to $491.8m, an increase of 0.2%. Underlying net profit after tax (NPAT) of $316.5m was down 1.3%. Basic earnings per share were down 1.4% to 65.4 cps and the dividend was also reduced by 1.3% to 39.2 cps, franked at 20%.

Looking at the operating divisions, Life Sciences revenue was $1,499m, up 12.4% with underlying EBITDA (EBIT before depreciation and amortisation) of $330.7m, up 9.2%. The equivalent numbers for Commodities were revenue steady at $1,086m and earnings up 1.6% to $383.9m.

However, the statutory accounts tell a very different story. Net Profit After Tax (NPAT) was down a massive 95.6% due primarily to a $278.3m impairment of the Nuvisan which was acquired only recently in 2021 in to expand the pharmaceutical business. More on that later.

Financial performance summary

(As at FYE)	2024	2023	2022	2021	2020
NPAT ($m)	12.9*	291.2	190.5	185.0	188.8
UPAT ($m)	316.5	320.6	264.2	172.6	127.8
Share price ($)	13.13	12.36	13.40	9.68	5.56
Dividend (cents)	39.2	39.7	32.8	23.1	17.6
Simple TSR (%)	9.4	-5	41.8	61	-24
EPS (cents)	2.7	60.2	39.5	35.8	26.5
CEO total remuneration, actual ($m)	2.346	1.189	3.976	2.987	2.649

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.

** Includes a non-cash impairment charge of $248.8 million in relation to the initial 49 per cent investment in Nuvisan.*

We queried ALS on a few items of interest in the accounts and received satisfactory responses.

- The apparent stalling of revenue growth in the commodities is primarily cyclical. The division was impacted by an extended slowdown in mining exploration due to soft capital markets.
- The 1.3% drop in underlying profit was driven by margin declines in pharmaceuticals due to subdued funding for new drug development, margin dilutionary impacts of recent acquisitions, lower volumes in geochemistry and unfavourable currency impacts.
- The decline in cash conversion performance from 97% in 2023 to 91% in 2024 can be attributed to positive growth in group revenue and the associated increase in working capital this generates. Also, there was the impact of the timing of the Easter holiday period delayed the March debtor collection cycle.
- The increase in intangible assets from $1.4b in 2023 to $1.5b in 2024 is explained by acquisitions made during the financial year. The intangibles, much of which are goodwill, are independently assessed each year and are not considered to be at risk of impairment.

Governance and culture

The ALS board has a good mixture of skills and experience. They publish a board skills matrix, but it is of the "collective skills" kind rather than showing the level of proficiency for each director. ASA would prefer a more detailed matrix.

The Chair, Bruce Phillips, believes that boards should be structured with 50% experience in a relevant industry and 50% in supporting areas such as finance, customer experience or law. Once Bruce retires there will be a deficit in the board's commodities experience and ASA would prefer the next NED appointment filled that gap.

Bruce commented that he doesn't agree with directors who collect a "portfolio" of board positions. He ensures his board members can comfortably manage their workload.

Key events

Without a doubt, the key event this year relates to ALS's investment in a European drug discovery and development company called Nuvisan. Half of Nuvisan was acquired in October 2021 for 145m EUR / $226.7m A$.

The initial rationale for acquiring Nuvisan was to expand the pharmaceutical business and establish a strategic footprint in Western Europe. However, as a minority shareholder, ALS struggled to implement changes they hoped would unlock value.

The Russian invasion of Ukraine had a significant impact on Nuvisan. Uncertainty caused by the conflict, impact on supply chains, inflation and interest rate rises led pharmaceutical companies to drastically reduce their R&D costs & risks. Nuvisan's revenue was particularly hard hit as pharma companies dialled back their drug discovery & development expenditure or shifted this work to locations outside Europe.

ALS still sees long term value in Nuvisan which generated revenue of ~$245m in calendar 2023. In March 2024 ALS announced the acquisition of the remaining 51% at nil cost. Accounting standards require a fair value adjustment process for the original 49% which has been completely written off resulting in an impairment of ~$258m.

With Nuvisan now fully under their control, ALS will now embark on a two year transformation program to unlock shareholder value.

It is important to note that the decision to acquire Nuvisan was made by the prior CEO, Raj Naran. And, according to ALS Chair Bruce Phillips, current CEO Malcolm Deane has taken decisive action to address the issues.

Key board or senior management changes

7 Jun 2023. Charlie Sartain retired as a Non Executive Director.

7 Jun 2023. Nigel Garrard commenced as a Non Executive Director.

19 Jan 2024. Luis Damasceno resigned as Chief Financial Officer (CFO).

1 Feb 2024. Stuart Hutton commenced as Chief Financial Officer (CFO).

8 Feb 2024. Nigel Garrard appointed Deputy Chair.

1 Mar 2024. Erica Mann commenced as a Non Executive Director.

31 Jul 2024. Bruce Phillips will retire as Chair, succeeded by Nigel Garrard.

Sustainability/ESG

ALS produce a very clear Sustainability Report with no hint of greenwashing. At the pre-AGM meeting Bruce Phillips told ASA that progress towards a more sustainable company has been a personal passion for many years. ALS global has been reporting on sustainability long before it was the norm to do so.

The company is making good progress on their climate change targets. This year they maintained carbon neutrality by installing more solar, buying renewable energy & offsetting emissions. The company has a goal of net zero by 2050 for scope 1, 2 & 3. They are taking deliberate steps to achieve this such as replacing gas ovens with electricity, adding more EV vehicles to their fleet and working with suppliers on reducing their emissions.

Their sustainability goals extend beyond climate change. For example, they are making a valuable contribution towards tackling antibiotic resistance which is seen as a huge, looming risk for humanity. They also have a good operational environmental record with no unresolved complaints, prosecutions or spills.

Their plans seem to be paying off with improving scores by multiple ESG rating agencies.

4. Rationale for Voting Intentions

Resolution 1. Election of Erica Mann as a director (For)

Erica Mann has extensive experience across complex, highly regulated environments in industries such as pharmaceuticals and fast moving consumer goods. She has experience with global and emerging markets across Africa, China, Russia and Brazil.

She currently holds non-executive director positions on the boards of Kellanova, previously Kellogg, (USA), DSM-Firmenich (Switzerland) and Perrigo (Ireland). She performs these roles remotely and is currently based in Sydney.

Her skills and experience seem a good fit for the ALS board and at our pre-AGM meeting Bruce Phillips was glowing in his praise for her. He is comfortable that her existing workload is not an impediment to carrying out her role on the ALS board.

Resolution 2. Adoption of Remuneration Report (For)

Last year, there was a first strike against the remuneration report due to shareholder concerns about the level of Long Term Incentive (LTI) payments to the former CEO, the use of board discretion and retention awards to secure the continued service of two key executives. Since then, the board has addressed some of these concerns.

- The former CEO's exit package has been renegotiated. He has forfeited his LTI payments in return for a reduced non-compete period.
- One of the two executives who was granted a retention award left the company and forfeited that bonus.
- The other executive remains employed and will receive the retention bonus. However, his Short Term Incentive (STI) has been reduced to zero so his total remuneration for the year is less than previously expected.

We will see at this year's AGM if the board's response is enough to satisfy those shareholders who voted for the first strike.

This year's remuneration report included some punitive outcomes in response to the Nuvisan impairment. Andreas Jonsson (GM Food & Pharma) had his STI reduced to 0%. The new CEO's STI was also adjusted downwards to 58% reflecting that he was not CEO at the time of the acquisition and has taken decisive action in relation to Nuvisan since taking the CEO role. Other executive STI outcomes averaged 40% of target. Board discretion was used to reduce these STI outcomes.

There were some items in this year's remuneration report that went against ASA's guidelines.

- STI is paid 70% in cash with the remaining 30% paid in equity, deferred for three years, with a financial gateway. ASA guidelines are for 50% in cash and 50% deferred for 12 months.
- LTI hurdles are measured over three years. ASA prefers four.

- LTI hurdles are based on underlying results rather than statutory results. This means the negative impact of the Nuvisan impairment is not reflected in the LTI hurdles.

The ALS Chair explained the rational for using underlying rather than statutory results when assessing LTI outcomes. If LTI is tied to statutory outcomes, then everyone is punished, not just those who were responsible for the negative issue. Bruce prefers to use underlying outcomes and board discretion to dial the remuneration down for those held accountable rather than to engage in “collective punishment” (my words, not his).

While we still have some concerns, on balance ASA will vote in favour of this resolution.

Resolution 3. Increase in fee pool for non-executive Directors (For)

ALS is seeking to increase the pool from which non executive director fees are paid. The pool was last increased at the 2022 AGM and currently sits at close to $1.9m. The proposed increase of just over $600k will take the fee pool to $2.5m. Currently director fees take up 89% of the pool and the ALS board would like headroom to facilitate board room succession, the appointment of an additional director and future fee increases.

Non-executive Director (NED) base retainer fees increased by 4.5% in FY24, reflecting CPI increases to remuneration across the ALS group.

External benchmarking confirms the proposed fee pool is at the median of comparable companies and NED fee growth is moderate, so ASA will vote in favour of this resolution.

Resolution 4. Approval of equity grants to Managing Director/CEO (For)

As the CEO is also a director, the board must seek shareholder approval for equity grants for the LTI plan. The company wishes to grant the CEO 163,082 performance rights totalling $1.5m US$ or $2.3m A$.

These rights are a fundamental part of the remuneration plan, which we support, so ASA will vote in favour of this resolution.

Resolution 5. Conditional resolution to hold a Spill Meeting (Against)

At last year’s AGM there was a 28% vote against the remuneration report resulting in a “first strike”. If this year’s vote on the remuneration report results in a “second strike”, this conditional resolution be voted on.

The resolution would call for a board “spill”, i.e. all board positions would be declared vacant, and shareholders would be asked to vote for any directors who wished to seek re-election within 90 days.

ASA’s voting guidelines state “ASA regards the decision to vote in favour of a board spill after a second strike to be a serious step, with a successful spill likely to be highly disruptive for a company. We are unlikely to support a board spill where a board has responded appropriately to shareholders dissatisfaction with the previous remuneration practice.”.

Given that the board has taken remedial action after last year's first strike, ASA will vote against this resolution if it is put to the meeting.

Appendix 1 - Remuneration framework detail

CEO rem. Framework for FY25	Target	% of Total Target *	Maximum opportunity	% of Total Maximum
Fixed Remuneration	1.75	31.0%	1.75	28.0%
STI - Cash	0.86	15.4%	1.29	21.0%
STI - Equity	0.37	6.6%	0.55	9.0%
LTI	2.63	47.0%	2.63	42.0%
Total	5.60	100.0%	6.21	100%

* 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. Some remuneration frameworks set a maximum opportunity amount, but not all.

For FY25, Malcolm Deane's fixed remuneration and allowances (TFR) have been increased to US$1.14m, which in the above table is converted to A$ at 0.65094 (exchange rate at 31 March 2024). The STI is 70% of FR at target and maximum opportunity is 105% of FR. 70% is paid in cash and the remainder in equity deferred for 3 years. ASA guidelines are for 50% cash, and a deferred equity of at least 12 months.

Positive features of the plan include variable remuneration clawback provisions for Malus and Code of Conduct circumstances, specific Code of Conduct KPIs in the STI; and a financial gateway ensuring the affordability of the STI to the company.