Charter Hall weathers economic headwinds

Company/ASX Code	Charter Hall Limited/CHC
AGM time and date	2.30pm AEDT Wednesday, 20 November 2024
Location	Level 20, No 1 Martin Place, Sydney (CHC Office)
Registry	Link Market Services
Type of meeting	In-person with webcast (no hybrid)
Monitors	Lewis Gomes and Partha Sarathy
Pre-AGM Meeting	David Clarke (retiring Chairman), Stephen Conry (Chairman elect), David Ross (Chair of Remuneration and Human Resources Committee) and Philip Cheetham (Head of Listed Investments)

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

1. How we intend to vote

No.	Resolution description	Voting Intention
1	Annual Report	Not for voting
2	Re-election of Directors (a) Ms Karen Penrose (b) Ms Jacqueline Chow	 For For
3	Adoption of Remuneration Report	For
4	Issue of Service Rights to Mr David Harrison	For
5	Issue of Performance Rights to Mr David Harrison	For
6	Remuneration of Non-Executive Directors	For
7	Capital Reallocation*	For

* Members attention is drawn to commentary in relation to this resolution below on potential tax consequences for security holders dependent on their own taxation circumstances.

2. Summary of Issues and Voting Intentions for AGM

- Interest rate increases have led to increasing capitalisation rates and falling property valuations resulting in reduced operating earnings and significant negative property revaluations.
- A number of CHC's listed investment trusts continue to trade at substantial discounts but have shown marked improvements during the early months of FY25 as has CHC's security price. As at 21 October, the security price for CHC was $16.17, a 45% increase of the closing FY24 price.
- One director is standing for election and another for re-election which the ASA will support.
- There are two remuneration resolutions in respect of the CEO Mr David Harrison which the ASA will support. There is also a resolution to increase the total fee pool for non-executive directors which the ASA will support.
- A resolution to reallocate capital between the parent company and the property trust is to be put to the AGM which will be supported by the ASA. There may be tax consequences for some securityholders if this reallocation, which will see a notional rather than actual payment of a franked dividend and return of capital, proceeds.

3. Matters Considered

Financial Statements

Charter Hall Group (CHC) is the parent company and manager of approximately 20 listed and unlisted Australian property trusts. CHC also invests, often with seed capital, in these trusts.

CHC recorded operating earnings post-tax of $359 million for FY24, down 19% on FY23. Statutory profit after tax including negative property revaluations was $222 million compared with $196 million for FY23. Distributions per stapled security were up 6.0% to 45.1 cents. Total funds under management (FUM) increased by $9.0 billion to $80.9 billion including CHC's 50% share of $15.4 billion of FUM managed by Paradice Investment Management (PIM). Property FUM at the end of FY24 was $65.5 billion, down $6.4 billion on FY23.

Like most property investment organisations, CHC has been adversely affected by a series of "higher for longer" interest rates leading to significant negative property revaluations as cap rates increased, while rising construction costs have adversely impacted development costs. Net fair value movements on investments and property for FY24 was negative $462 million plus another negative $119 million on "other non-operating items" to result in the statutory loss of $222 million mentioned above.

Investment management revenue was down 25% to $352 million while property services revenue was stable at $107 million for FY24. Funds management EBITDA margin dropped from 73% to 68%. Net finance costs increased by 31% to $106 million.

CHC's investments in its own funds for FY24 was $2.76 billion, down $0.19 million from FY23, and approximates only 4.2% of total property funds under management which demonstrates the leverage it receives from managing externally sourced capital. The property investment yield across the group was about 4.7% for FY24 up from 4.4% in FY23. Its NTA at 30 June 2024 was $5.49 per security ($6.28 at 30 June 2023) and its balance sheet gearing was 3.0% (2.2% at 30 June 2023), although the "look through" gearing including that within its funds increased to 37.8% from 33.6%.

CHC has provided guidance for FY25 of post-tax Operating Earnings Per Security (OEPS) of approximately 79 cents and a distribution per security of 47.8 cents, some 6% above that for FY24.

5 Year Financial Performance

(As at FYE)	**2024**	**2023**	**2022**	**2021**	**2020**
Statutory Profit ($m)	(222)	196	911	477	346
Operating Earnings ($m)	359	441	543	284	323
Share price ($)	11.18	10.73	10.83	15.52	9.69
Distribution (cents)	45.1	42.5	40.1	37.9	35.7
Simple TSR (%)	8.4	2.8	(27.6)	64.1	(7.2)
Operating EPS (cents)	75.8	93.3	115.6	61.0	69.3
CEO total remuneration, actual ($m)	5.960	3.834	9.815	5.250	8.499

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. CEO total remuneration above is based on actual remuneration received during the year with any rights that were vested calculated based on closing share price on the date of vesting. Executives can voluntarily defer cash component of STI and such deferrals are not included in the actual remuneration until they are exercised.

Governance and culture

CHC has a board of 7 directors including David Harrison as CEO and MD, of whom 2 are female. The management team comprises 9 personnel, including the CEO, of whom 3 are female. There are 3 "reported executives" being the CEO plus 2 others (one male and one female). Clearly CHC has some way to go to achieve something resembling gender parity.

It is noted that there is no skills matrix provided in the Annual Report and the link included in the corporate governance report is only to the corporate governance section of the website. It can be found and then seekers of the matrix have to navigate to the CHC section of the website and the Charter Hall Group Board and Committee Details section. It shows aggregate skills and doesn't identify which director holds which skill. Information can be gleaned from the word descriptions given in the Annual Report and in Notices of Meeting which for CHC are quite comprehensive.

Non-executive directors are expected to hold shares in the company equivalent to the value of one year's directors base fee within 3 years of appointment. Two of the longer serving directors still have quite low shareholdings in CHC, namely Mr Greg Paramor who joined the board in November 2018 (14,300 shares) and Mr David Ross who joined the board in December 2016 (17,500 shares). The standard member fee (excluding committee fees) for a CHC director is $186,559 which, based on the share price at 30 June 2024 of $11.18, would equate to 16,690 shares. Mr Ross just meets this limit while Mr Paramor falls short but we are advised he has substantial investments in CHC funds. Ms Chow joined the board in February 2021 and is currently reported to hold only 10,000 shares. We understand that there may be personal reasons for this situation.

PricewaterhouseCoopers (PwC) has been the auditor for CHC for many years. The Annual Report (Page 112) advises total fees paid to PwC for FY24 was $541,355 for audit services and $313,732 for non-audit services comprising $61,732 for taxation compliance services and $252,000 for "sustainability assurance services". We are advised that the new CFO is reviewing the current role of PwC but no changes have been contemplated to date.

Key events

There were no significant key events during FY24.

Key board or senior management changes

CHC Chairman Mr David Clarke recently announced his pending retirement from the board to take up the role of chairman of ASX Limited. Mr Clarke will retire at the end of this year's AGM after 10 years as Chairman. He will be replaced as chair by Mr Stephen Conry AM, a current Non-Executive Director of Charter Hall who joined the board in January 2023.

Ms Karen Penrose was appointed a director of CHC from 1 November 2024 and will stand for election at the AGM.

In late 2023 CHC announced the resignation of its CFO Russell Proutt and he ceased employment on 29 February 2024. Anastasia Clarke was appointed as his replacement in September 2023 and commenced in the role of CFO on 29 January 2024. Ms Clarke was until recently the CFO at GPT Group and prior to that worked for Lendlease and Dexus.

Sustainability

CHC provides a comprehensive Sustainability Report on Pages 32 to 39 of the Annual Report. Highlights include a 71% reduction in Scope 1 and 2 emissions against a FY17 baseline, 81% renewable electricity applied to its assets underpinned by a long-term PPA, 80MW of onsite solar installed Group-wide (an uplift of 23% on FY23) of which 77% supplies tenants with clean energy.

In terms of its property holdings, it has achieved 5.0 Green Star Performance for 93% of its eligible assets within its Office portfolio, 3.0 Green Star Performance against 100% of eligible assets within its Retail portfolio and 2.0 Green Star performance for 71% of its Industrial and Logistics portfolio.

3. Rationale for Voting Intentions

Resolution 2 (a) Election of Ms Karen Penrose as an Independent Non-Executive Director

Ms Penrose has extensive executive experience in financial services, property, health, resources and energy. Her career includes 20 years in banking with CBA and HSBC and 8 years as a listed-company CFO. She is currently a non-executive director of Ramsay Health Care, Bank of Queensland and Cochlear Limited. Further details of Ms Penrose's experience are available in the Notice of Meeting.

Ms Penrose appears to be well suited to the role of a director of CHC and the ASA will be voting all undirected proxies in her favour.

Resolution 2 (b) Re-election of Ms Jacqueline Chow as an Independent Non-Executive Director

Ms Chow has over 23 years of corporate experience in executive and non-executive positions in general management, strategy, marketing and technology across a range of sectors including industrial, retail, telecommunications and financial services.

Other than her low shareholding, Ms Chow appears to be well suited to the role of a director of CHC and the ASA will be voting all undirected proxies in her favour.

Resolution 3 Remuneration Report

The Remuneration Report is well set out in the Annual Report and the framework for the CEO is set out in the table of Appendix. 1 The framework is typical of most ASX companies in that it has a Fixed Annual Remuneration (FAR), a Short Term Incentive (STI) and a Long Term Incentive (LTI). A financial gateway of 95% of target Operating Earnings Per Security (OEPS) set by the board must be met before any STI entitlement is available. The STI is delivered 67% in cash and 33% in deferred service rights The LTI is based 50% on reaching an OEPS target and 50% on reaching a TSR target. Details are provided in the Annual Report. The ASA does have a preference for the STI to be split evenly (50%/50%) between cash and rights rather than the CHC mix of 65%/35% but does note that the FR is modest compared with other similar companies.

For FY24 there were no changes to the FAR for the CEO but the CIO and former CFO received increases to FAR of 8.1% and 4.0% respectively. For the CEO the FAR remains at $1,500,000 while the maximum STI is 150% of the STI target of $2,486,250. The maximum LTI for the CEO is 200% of FAR or $3,000,000 which brings his Total Target Remuneration (TTR) to $6,986,250 for FY24. His actual received remuneration for FY24 was $5,960,604 or 85% of his TTR.

There was an approximate 3.5% increase in fees paid to NED's (refer Page 76 of the AR).

In summary, the ASA believes the remuneration framework is reasonable and recognises the difficulties of the past year while also acknowledging the need to reward and incentivise key executives and staff. The ASA will therefore vote all undirected proxies in favour of this resolution.

Resolution 4 Issue of Service Rights to Mr David Harrison

These rights arise from the deferred allocation of the STI award for the CEO for FY24. The number of service rights has been determined on a face value basis by dividing the value of the deferred portion of the STI award of $828,750 by the VWAP for the month of June 2024 of $12.13 resulting in 68,322 service rights being awarded.

Given the ASA's support for the Remuneration Report, we will vote all undirected proxies in favour of this resolution.

Resolution 5 Issue of Performance Rights to Mr David Harrison

These performance rights are issued in respect of the LTI award for the year ending June 2025. The number of rights is calculated by dividing the LTI Opportunity of $3,000,000 by the VWAP for June 2024 of $12.13 yielding 247,320 rights. The rights have a four year testing period and further details are provided in the Annual Report and Notice of Meeting.

Given the ASA's support for the Remuneration Report, we will vote all undirected proxies in favour of this resolution.

Resolution 6 Remuneration of Non-Executive Directors

This resolution seeks to increase the maximum aggregate sum which may be paid to non-executive directors (NED's) by $500,000 per annum to a maximum of $2.5 million. The current annual fees payable to the 6 NED's totals $1.9 million which is close to the current approved limit.

To enable some headroom for possible further directors or fee increases, this increase seems reasonable and the ASA will therefore vote all undirected proxies in favour of this resolution.

Resolution 7 Capital Reallocation

The purpose of this resolution is to enable a reallocation of capital between Charter Hall Limited (CHL) and Charter Hall Property Trust (CHPT). The proposal is to allow the transfer of up to $400 million of CHL's capital to CHPT prior to 30 June 2025. This would result in a reallocation of capital withing the Charter Hall Group (CHC) being 23.8% in CHL and 76.2% in CHPT. Further details of the proposal are presented in the Notice of Meeting which stresses that "no payment of any cash will be made to CHL shareholders nor will any CHL shares or CHPT units be issued or cancelled". Furthermore, no cash payments are proposed to be made to security holders in relation to this proposal and it will "in no way limit Charter Hall Group's ability to pay dividends in the ordinary course, including special dividends".

Resolutions 7.1 and 7.2 need a special majority (ie. 75% or more of the votes cast by securityholders who are entitled to vote) as they amend the constitutions of CHL and CHPT, while Resolution 7.3 only needs a simple majority. The Explanatory Memorandum (EM) states that CHC intends to commence early engagement with the Australian Taxation Office (ATO) to reach a settled position in relation to tax implications for securityholders and will update on the outcome via a market announcement. The board does not need any further approval including for declaration of special dividend from CHL to CHPT.

The mechanism mentioned above does not afford ASA members an opportunity to consider the outcome of the ATO engagement prior to voting on the resolutions, which is not practical under the circumstances. Even though the EM provides an analysis of the potential tax consequences on securityholders, the ASA cannot be certain that there will not be unintended impacts on some members from the capital reallocation (as an example, anyone with a marginal tax rate of over 30% may be required to pay a cash 'top up' tax above their imputed franking credit as a result of this resolution). While ASA will vote all undirected proxies in favour of the resolution, it urges members to consider their personal circumstances and direct their proxies accordingly.

Appendix 1
CEO remuneration framework detail for FY24

Rem Component	Target* $m	% of Total	Max. Opportunity $m	% of Total
Fixed Remuneration	1,500,000	21	1,500,000	18
STI - Cash	1,658,329	24	2,487,493	30
STI - Equity	827,921	12	1,243,747	15
LTI	3,000,000	43	3,000,000	37
Total	6,986,250	100	8,229,375	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.

For FY24, the financial gateway for the STI award was 70.775cps (95% of target OEPS of 74.5cps set by the board) which was exceeded with an achieved OEPS of 75.8cps. Of the eight STI metrics, the outcomes met or exceeded expectations for all except one which did not meet expectations. Nevertheless, the board decided to exercise its discretion and award the full 100% of the target STI award (refer Pages 64 and 65 of the AR).

The LTI vested awards for FY24 comprised the FY20 Tranche 2 which vested on 31 August 2023 at 87.5% of issued performance rights. The FY21 LTI which vested on 31 August 2024 at 93.75% of issued rights will be included in the actual remuneration for FY25 (refer Pages 71 and 72 of the AR).