OR

Hungry for success or a self-entitled fat cat. You choose.

“Show me the incentive and I’ll show you the outcome” The late, great Charlie Munger. Never a truer word spoken.

A few weeks ago in the US, a Delaware judge ruled that an incentivisation scheme earned by Elon Musk, CEO of Tesla, was to be rescinded.

In her 200-page opinion on Jan. 30, Chancellor Kathaleen McCormick called the pay plan the largest in public corporate history, and said it was agreed upon by people “who were beholden to Musk.”

Understandably Musk fired back. “Never incorporate your company in the state of Delaware” he wrote on his social media platform X. He also said he would hold a shareholder vote to move the Tesla site of incorporation to Texas.

So why is this a big deal? Because the judge’s decision was short sighted, political and will have significant ramifications on public markets.

The case

An investor named Richard Tornetta sued Musk and several Tesla directors in 2018, claiming Musk's pay package was unfair. Mr Tornetta owns a mere 9 shares in Tesla. And for what it’s worth, he made 10 times his money anyway, but we’ll get to that.

The pay plan had the potential to generate a staggeringly large amount of money for Musk, which from my perspective is academic, because he had to achieve the near impossible to get it which would benefit all involved; and if he didn’t, he got nothing.

Time has shown he did of course achieve the impossible. Not only did he clear the first hurdle by meeting 4 consecutive quarters of EBITDA and revenue targets, he also grew the market value of Tesla by 10 times (1000%).

Ultimately, the package had been approved by the board and has resulted in spectacular wealth generation for shareholders, but still, people think it is unfair.

The plan was also approved by 73% of all shareholders, excluding Musk’s own and family votes.

Shareholders loved the deal.

Such is the nature of big business these days, it reeks of politics. Musk has been the victim of a number of politicised witch hunts recently, the most absurd being a claim by the US Justice Department and Securities Exchange Committee (SEC) in August last year claiming that Musk used company funds to build a glass house.

Even the current sitting US President stated in a Washington press conference in 2022, that Musk’s ties to foreign countries are ‘worth looking at.’ Meanwhile, Musk has quietly provided free internet to all of Ukraine via his vast Starlink network, to no fanfare nor press. Free, unlike the US industrial military complex that is selling bombs and bullets to Ukraine for literally ten times the cost it is produced by their opponent, Russia. Dining off the misery of others.

Alas, as per usual, I digress.

In the case, the claim has been made that Tesla’s directors breached their fiduciary duties by awarding Musk ‘a performance-based equity-compensation plan.’ How absurd. That is precisely how all executives should be remunerated, tying the shareholders’ interests with the executive’s actions.

The plan

Under the plan, Musk had the opportunity to secure 12 tranches of options, each representing 1% of Tesla's total outstanding shares as of January 21, 2018. To be exercised each tranche would require a further $50 billion increase in Tesla value.

The share price of Tesla on January 21, 2018 was around $23. The current share price is $200 - noting it almost hit $400 in 2021.

That is truly the most heroic compensation plan I've ever seen, and yes, justifiably large if achieved. It was all stock, no salary, no cash. No one loses here.

Back in 2018 when the payment plan was created, Tesla was not doing particularly well, the production line was riddled with problems, amongst a multitude of other issues. At the time Musk himself said he was sleeping on the floor of the factory. The concept of lifting the share price that far was outlandish, almost comical. Even if he doubled the value of Tesla from that point, he would have received nothing, as it wasn't sufficient to reach the hurdle rates.

So, what was the value of the package? $56billion, a dirty big number. But of course, the rest of the shareholders made half a trillion.

You could count on one hand the number of executives that would back themselves so bravely. Massive potential upside if one shoots the lights out, but no safety net.

This appalling decision by the court will result in the removal of incentive plans from public markets, and with it, the best and smartest operators that we investors want exposure to. Why would they bother?

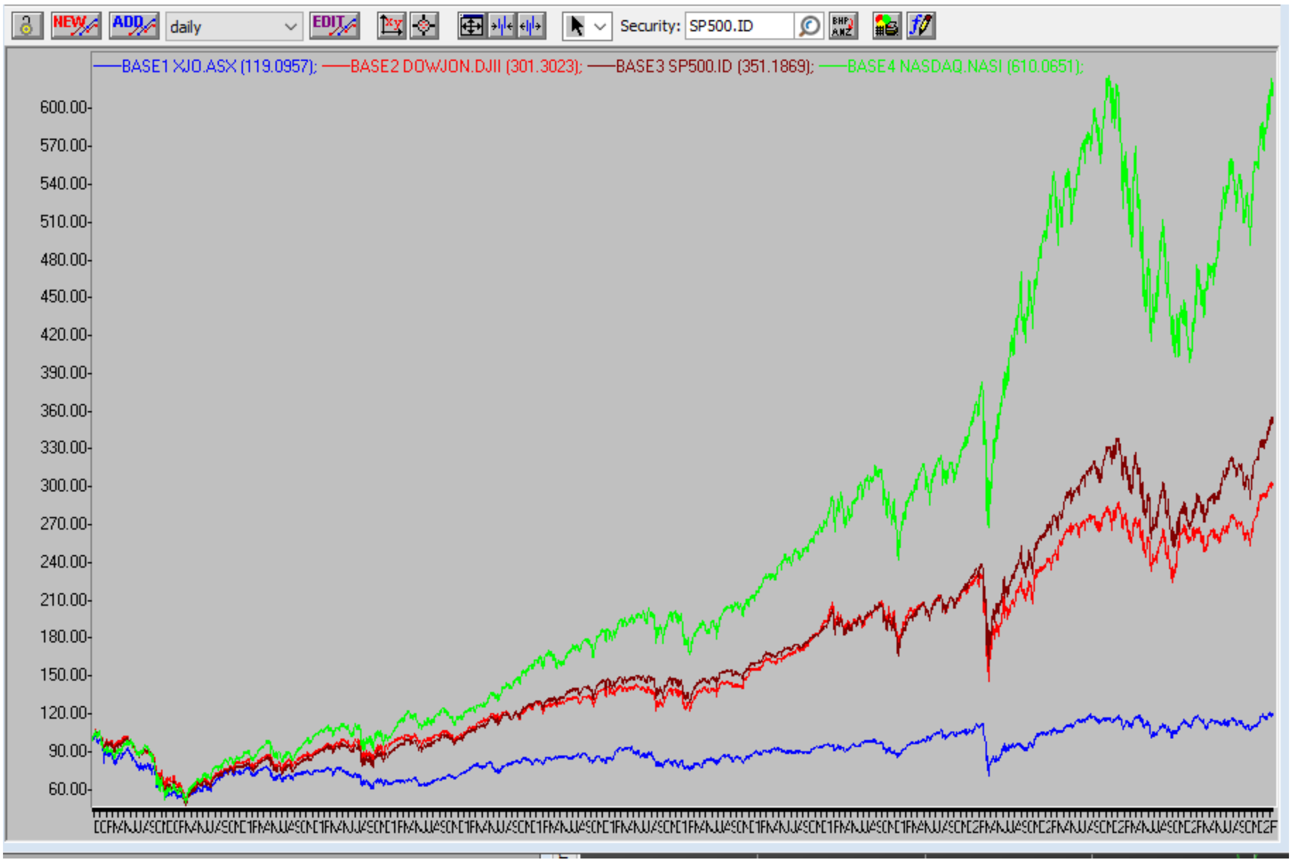
To quote David Sacks, venture capitalist and podcast host, *"Most CEO's work their way up the corporate ladder, and then they pay themselves huge amounts of money, regardless of whether the company succeeds or fails. And that's the deal they want because they don't have confidence in themselves to deliver what Sorkin called the crazy outcome."*

"While Elon was spending the last 6 years making Tesla go 10 x, let's look at GM (General Motors - direct competitor to Tesla)….Mary Barra (CEO of GM) was paid roughly $200m over the last five years, and the stock price is literally the same price it was five years ago."

$200m is massive, truly gigantic, and for achieving mediocrity. If company executives are going to be paid these exorbitant numbers, the least they could do is make their shareholders some money.

The vast majority of executives of the largest listed Australian companies are not correctly incentivised either- i.e. aligned with shareholders - which is why the majority of large Australian companies have not, do not and will not ever outperform.

If you don't believe me, below is the performance of the NASDAQ, S&P500, Dow Jones and ASX200 since the GFC. Guess which line is the ASX200??



BHP

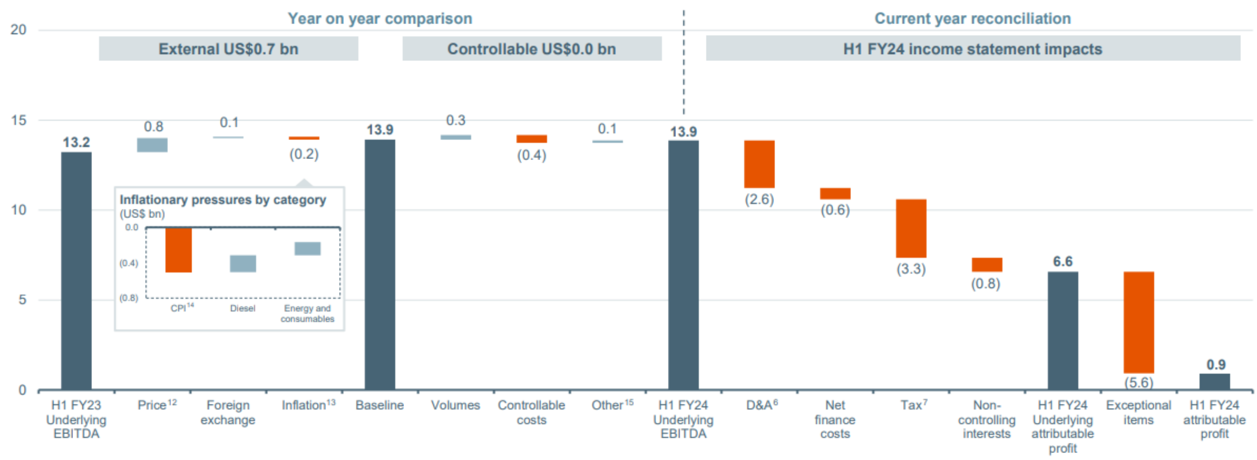
1H24 Results

- NPAT of US$927m, down 86% on 1HFY23 **post US$5.7b of exceptional losses at NickelWest and Samarco** (as reported last week).
- Underlying revenue US$27.2bn vs consensus US$26.9bn
- Underlying EBITDA of US$13.9bn vs consensus US$14.0bn
- Underlying NPAT of US$6.6bn vs consensus US$6.6bn
- Basic EPS of 130 UScps vs consensus 130 UScps
- Dividend of 72 UScps vs consensus 70 UScps
- Net debt US$12.6bn (vs US$6.9b H1-FY23) noting US$5-15b target range.
- Underlying NPAT in-line with prior period with US$2.5b nickel west impairment and US$3.2b Samarco dam failure.
- Unit costs ~5.4% higher across major assets noting normalisation of commodity linked consumables (diesel and acid).
- Capex guided to ~US$10b FY24/FY25E and ~US$11b medium term as copper and potash project spend lifts.
- BHP view the near-term economic outlook for the developed world improving modestly with China and India to remain a relative source of stability for commodity demand.

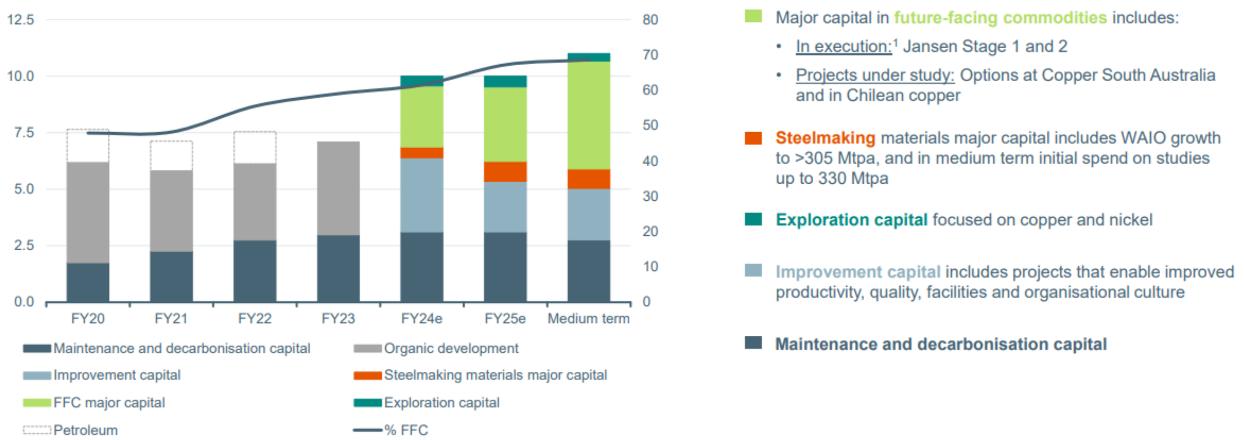
Key group metrics

	HY24 US$M	HY23 US$M	Change %
Revenue	27,232	25,713	6%
Profit from operations	4,803	10,833	(56%)
Attributable profit	927	6,457	(86%)
Basic earnings per share (cents)	18.3	127.5	(86%)
Interim dividend per share (cents)	72	90	(20%)
Net operating cash flow	8,884	6,770	31%
Capital and exploration expenditure	4,744	3,027	57%
Net debt	12,648	6,910	83%
Underlying EBITDA	13,875	13,230	5%
Underlying attributable profit	6,569	6,597	(0%)
Underlying basic earnings per ordinary share (cents)	129.6	130.3	(1%)

Earnings variance and drivers
(US$ bn)



Increasing spend on future-facing commodities to ~70%
(US$ bn, nominal) (capital in future-facing commodities, %)



Note: Medium term refers to FY26 – FY28 average. FFC – future-facing commodities. Major capital represents projects >US$250 m.
1. BHP is currently assessing phasing and capital spend for the development of the West Musgrave project as part of a review of the development plans for Western Australia Nickel.

- It is worth mentioning a few points about the Nickel West business, and indeed, nickel as a whole. Despite the costly US$2.5b writedown, the business is still worth keeping, even though right now, the operations are uneconomic.

Nickel

Production:	39.8 kt
Average realised price:	US$18,602/t
EBITDA margin:	(24)%

- Nickel is a stunningly volatile commodity between periods of inactivity, as illustrated in the chart below:

- And as you can see, just before the GFC, nickel was trading over US$50,000.
- Currently losing US$50-$100m p.a., if BHP chose to sell Nickel West, the cost of effecting the sale would be around US$1bn- going to site clean up and reparations, etc. If, however, they just hang on and bear the US$50-US$100m losses over a small period of time, when the price spikes, they make hay; very quickly. Don't forget alongside all of the other standard uses of the metal- stainless steel, nickel alloys, magnets, etc, - it is also a key component in nickel-cadmium (NiCd) and nickel-metal hydride (NiMH) batteries.
- Looking at BHP's asset trading history, they may well sell it now at a low point...

Bendigo Bank (BEN)

1H24 Result:

- Pre-Provisioning Operating Profit (PPOP) $424M, in line with consensus.
- Loan impairment expense of $11M (that's amazing).
- NPAT $268M (in line with cons $263M) and EPS 47.4cps, ~2% ahead of cons 46.3cps.
- Interim Dividend of 30c per share, in line with consensus.

- Net Interest Income (NII) -4.3% HoH to $798M, 2% softer than cons, with NIM -15bps to 1.83% (post revenue share agreement) due to price competition in both lending and deposits, and a higher level of liquid assets. **That's a very skinny margin, very little margin of error.**
- Total revenue $1.0B, (7% above consensus).
- Costs -4% HoH a good result, but +14% YoY. Costs 12% above cons.
- Cash ROE of 7.82% (down from 8.45% in 2H 23).
- CET1 ratio 11.23%, slightly below cons 11.6%.
- Homesafe in run-off from 1 Jul 24; income will reduce over time subject to rate of and profit on completions.
- **Bluurghh, although asset quality is good, indicating minimal impairment risk ahead.**
- **BEN looks cheap but there's no growth and it is operating on skinny margins. Better value elsewhere.**

Highlights (A$m)	06/21	06/22	06/23	06/24E	06/25E	06/26E	06/27E	06/28E
Revenues	1,805	1,710	1,920	1,916	1,880	1,868	1,857	1,846
Pre-tax profit	754	702	725	779	757	782	820	820
Net earnings (reported)	457	500	577	548	533	513	537	537
Net earnings (UBS)	524	488	497	538	523	540	566	566
Tier 1 ratio %	11.6	11.6	13.4	14.1	14.3	14.7	15.0	15.4
EPS (UBS, diluted) (A$)	0.83	0.78	0.79	0.81	0.78	0.81	0.84	0.84
Profitability/valuation	**06/21**	**06/22**	**06/23**	**06/24E**	**06/25E**	**06/26E**	**06/27E**	**06/28E**
ROE (UBS) %	8.6	7.5	7.3	7.7	7.3	7.3	7.4	7.2
P/PPOP (diluted) x	7.4	9.3	8.0	7.5	7.7	7.7	7.8	7.8
P/BV x	0.7	0.8	0.8	0.8	0.8	0.8	0.7	0.7
P/BV (UBS) x	1.0	1.1	1.0	1.1	1.1	1.0	1.0	0.9
P/E (UBS, diluted) x	10.5	12.5	11.5	12.2	12.6	12.3	11.7	11.8
Dividend yield (net) %	5.8	5.5	6.7	5.9	5.7	5.4	5.7	5.7

Source: Company accounts, LSEG Eikon, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of A$ 9.89 on 16-Feb-2024

22nd February 2024

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Click on the link below to read:

EFG Inview – February 2024 – Global House View & Investment Perspectives - - 22 Feb 2024

Have a good weekend.

Ben and the team.

This report has been prepared by Ben Morrissey
Shaw and Partners, Morrissey Wealth Management
Level 36, 120 Collins Street
Melbourne VIC 3000