

Statement in relation to The UK Corporate Governance Code (July 2018): Board Leadership and Company Purpose, Provision 4

Dear Shareholder

I am writing to you in my capacity as the Chair of the Remuneration Committee (the “Committee”) of Pendragon plc (the “Company”) to provide an update on the Company’s response to the outcome of the 2020 Annual General Meeting (“AGM”) in May this year. We note that all resolutions were successfully passed with the requisite majority, although there were four resolutions which received less than 80% of votes in favour.

I would like to set out, based on my communications with shareholders prior to the AGM and reflecting on views expressed at the AGM, what I understand to be the reason for the voting outcomes, as well as the actions taken in response to them.

Resolutions 3 and 4 - Directors’ Remuneration Policy and Long Term Incentive Plan

The Committee is aware of the increasing focus on remuneration and governance from the Company’s shareholders and as such the Directors’ Remuneration Policy (the “Policy”) which was put to shareholders at the 2020 AGM contained a number of best practice features including:

- A move away from the one-off Value Creation Plan to a more conventional Long Term Incentive Plan (“LTIP”) with a performance period of 3 years and a holding period of 2 years (in normal circumstances);
- Improved malus & clawback provisions including the addition of reputational risk and corporate failure to the triggers;
- Introduction of a post-cessation shareholding requirement equal to the in-employment shareholding requirement for 2 years after cessation of employment; and
- Changes to the pension policy to bring Executive Director pensions in line with the average employee rate over time by ensuring that new Executive Directors are appointed with a pension contribution which is not above the level available to the wider workforce and reducing the pension contribution of current Executive Directors where appropriate.

The binding resolutions to approve the Policy and the LTIP received 58.70% and 58.10% of votes in favour respectively and the Committee believes that the primary reason for the voting outcome on the Policy was due to the LTIP.

Specifically, the possibility to make exceptional awards of up to 250% of salary was a concern for shareholders. The rationale for the enhanced 2020 award was that the CEO and CFO did not have the opportunity to take part in a long-term incentive arrangement upon joining the Company as there was not a relevant structure in place at their respective joining dates in 2019. As such, it is intended that subsequent awards under this Policy will be made at the normal maximum level.

The other facet of the LTIP which some shareholders raised concerns with was the ability to apply a performance period of 1-year in exceptional circumstances. The normal practice under the Policy is for 3-year targets to be set, however given the difficulty in setting 3-year targets in particular for the FY20 award, the Policy contained the flexibility in exceptional circumstances to award an LTIP with a performance period which is shorter than 3 years.

The Committee believes that going forward the Policy will continue to serve as an effective tool to retain and motivate its key talent which in many core aspects is aligned with best practice governance.

The next section of this statement sets out the proposed implementation of the LTIP for 2020 and the considerations made by the Committee to ensure that the award is fair as well as serving as an effective incentive.

Resolution 2 - Directors' Remuneration Report

The advisory vote on Pendragon's Remuneration Report (the "Report") was passed by shareholders at our AGM in May 2020 with support of 78.48% of votes in favour of the resolution. The Company understands that this outcome was attributable to the following decisions:

- The exceptional LTIP award proposed for the new CEO and CFO for FY2020 based on a one-year performance period;
- The salaries for the new CEO and CFO; and
- Payments to departing Executive Directors.

Taking each of these in turn, the Committee recognises that some shareholders were not supportive of the proposal to award an exceptional LTIP of 250% of salary to the new CEO and CFO. As a result of conversations both internally and with shareholders after the AGM in May, the Committee determined that it was not possible or appropriate in the wake of the COVID-19 pandemic to make an LTIP award due in part to the uncertainty of setting targets and instead decided to defer its decision making until a later date. When more clarity emerged going towards the end of Q3, the Committee determined to make the following appropriate and proportionate adjustments to the original proposal, all of which remain in line with the Policy:

- Set a performance period which runs to the end of FY2021 rather than the initially planned FY2020. It became increasingly difficult to set targets against an uncertain macroeconomic backdrop and the Committee felt that waiting longer meant a shorter period between the setting and measurement of targets. As such, the Committee determined that measuring performance to the end of FY2021 was more appropriate.
- The Committee has adapted the LTIP such that 50% is measured on EPS and 50% on strategic measures whereas the original proposal was that 100% would be measured on EPS. The introduction of strategic metrics achieves two key goals:
 - Allows measurement of progress towards vital imperatives drawing a direct link between the strategy set out to shareholders at the start of September and the incentives; and
 - Ensures that the LTIP does not pay-out on a single metric which could lead to all-or-nothing payments depending on the setting of the targets.
- The Committee has continually monitored the Company's share price since the AGM for the purposes of determining the level of awards. The average share price over the month of February 2020 was 12.365p and is an indicator of the share price before the COVID-19 impact. The Committee determined that were the share price to be significantly below the February share price then a reduction to the number of awards would be made to protect against windfall gains. However, the share price reacted positively to the Q3 results announcement and at the date of grant the share price was 14.084p and therefore the Committee determined that such adjustment was not necessary.

Secondly, the Committee understands that some shareholders highlighted that the base salary levels of the new Executives were above that seen for other companies of a similar size. The Committee considers a range of reference points when determining salaries including size as well as sector comparators. The

Committee seeks to attract the right talent to the business and always ensures it is paying the right amount for the right candidate. As per the Policy, any future increases will typically be made in line with those to the wider workforce.

Lastly, with regards to the payments to the former Executive Directors, these were one-off payments for departing Directors which were made in line with the approved remuneration policy at the time and the majority of the sums were linked to contractual payments in lieu of notice. Naturally, the Committee does not foresee such payments in the future.

Resolution 11 - Re-election of Michael Wright

The Company understands that the reason for the 65.79% of votes in favour of Resolution 11 (my re-election) at the AGM this year was linked to the other remuneration related resolutions stated above.

Next steps

After considerable evaluation, the Remuneration Committee believes that the core issues with the negative votes were:

- One off in nature, such as payments to departing directors or appointments of new directors; or
- And in the case of the LTIP, clearly demonstrable that the Committee has taken steps to address shareholder concerns.

I am pleased that the majority of shareholders supported the resolutions, and I will continue to communicate with all shareholders on behalf of the Committee and invite you to get in touch with any comments or questions.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Mike Wright', is positioned above the printed name.

Mike Wright - Chair of the Remuneration Committee

04 November 2020