

REPORT ON OPERATIONAL AND FINANCIAL PERFORMANCE

OF THE TRANSPOWER GROUP FOR
THE THREE MONTH PERIOD ENDED
30 SEPTEMBER 2011

T R A N S P O W E R



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Transpower is the State Owned Enterprise that plans, builds, maintains and operates New Zealand's high voltage electricity transmission network – the National Grid – which links generators to distribution companies and major industrial users.

Introduction

This is the second quarterly report produced by Transpower.

The report summarises the unaudited financial results of Transpower for the three months ended 30 September 2011, together with the results for the comparative prior-year period.

The report also sets out year to date progress against Transpower's Statement of Corporate Intent (SCI) performance targets.

These quarterly reports provide readers with financial and operational information between the publication of the interim and annual reports.

We welcome your feedback on this report and trust that you find it useful. Feedback should be sent to communications@transpower.co.nz.

Update on Transpower's operations for the three months ended 30 September 2011

Financial Performance

Net profit after tax for the period to 30 September 2011 before net changes in financial instruments was \$42.1 million compared with \$42.4 million for the previous corresponding period.

Transmission revenue increased in the period by 6 per cent to \$173.3 million.

Expenses increased by 5 percent to \$65.3 million.

Net finance costs increased in the period by 6 per cent to \$20.7 million reflecting an increase in debt as Transpower funds its substantial capital programme.

Total capital expenditure, excluding freehold property purchases, was \$194.6 million, an increase of \$91 million over the previous corresponding period. The increase is driven by expenditure on the North Island Grid Upgrade (NIGU) project and the HVDC upgrade project (Pole 3).

Operational Update

Grid reliability was better than plan, despite the severe snowstorms which hit both islands in August.

Construction work on the North Island Grid Upgrade (NIGU) project is progressing satisfactorily. All easements have been secured.

Pole 3 is scheduled to be available for operation from December 2012.

Construction work on the North Auckland and Northland project has begun.

An appeal against the planned new Wairakei to Whakamaru Replacement Transmission Line project was withdrawn in August, the consents are thus final.

The \$20 million West Coast Upgrade project, the new Reefton to Dobson 110 kV transmission line, was commissioned successfully in September.

In August, the Commerce Commission approved Transpower's operating and capital expenditure requirements plan for the period 2012/13 to 2014/15. The amounts approved were essentially the same as Transpower's proposals.

Transpower continues to access debt capital markets to fund the significant build programme and to replace maturing debt. In September, a US Private Placement secured long-term funding of \$466 million. The funding is due for settlement in October.

Statement of Corporate Intent Measures (refer to table on page 11)

Transpower is on target to achieve the majority of its SCI performance measures.

Financial measures

Year to date financial performance is ahead of plan which is reflected in favourable financial measures (including operating profit margin, return on capital employed, return on equity and interest cover).

Non-financial measures

One target is at risk. By 30 September, 15 medical treatment injuries had been recorded against an SCI target of <26 for the full year. While the injuries were mostly minor, and reflect the greater volume of work underway, we are committed to improving the safety of all our operations.

Other non-financial measures are on target.

Operational measures

Targets for customer reliability are all on target.

Consolidated statement of comprehensive income

For the three months ended 30 September 2011

		UNAUDITED	UNAUDITED	AUDITED
	NOTES	3 MONTHS 30 SEP 2011	3 MONTHS 30 SEP 2010	YEAR 30 JUN 2011
		\$M	\$M	\$M
Operating revenue				
Transmission revenue	2	173.3	164.1	675.3
Other revenue	2	13.9	14.5	56.1
Finance revenue	4	0.1	0.1	5.8
		187.3	178.7	737.2
Operating expenses				
Transmission expenses	3	28.9	28.9	141.0
Employee benefits	3	14.8	13.8	56.4
Other operating expenses	3	21.6	19.5	81.8
		65.3	62.2	279.2
Earnings before interest expense, tax, depreciation, amortisation, impairment and changes in the fair value of financial instruments				
		122.0	116.5	458.0
Depreciation		39.0	33.3	146.4
Amortisation		3.1	3.3	14.3
Impairment		–	–	19.7
Asset write-offs		0.7	–	12.5
Finance expenses	4	20.8	19.6	87.3
Earnings before changes in the fair value of financial instruments and tax				
		58.4	60.3	177.8
(Gain) loss in the fair value of financial instruments		74.4	77.2	65.4
Earnings before tax				
		(16.0)	(16.9)	112.4
Income tax expense (credit)		(4.5)	(5.1)	33.9
Net profit (loss)				
		(11.5)	(11.8)	78.5
<i>Total net profit (loss) for the period is attributable to:</i>				
Non controlling interest (NCI)		(5.0)	0.5	6.5
Owners of the parent		(6.5)	(12.3)	72.0
		(11.5)	(11.8)	78.5
Other comprehensive income for the period net of tax				
		–	–	–
Total comprehensive income for the period				
		(11.5)	(11.8)	78.5
<i>Total comprehensive income for the period is attributable to:</i>				
Non controlling interest (NCI)		(5.0)	0.5	6.5
Owners of the parent		(6.5)	(12.3)	72.0
		(11.5)	(11.8)	78.5
<i>Reconciliation of net profit (loss) specifying the net impact of fair value movements</i>				
Earnings before changes in the fair value of financial instruments and tax				
		58.4	60.3	177.8
Income tax expense (credit) excluding changes in the fair value of financial instruments		16.3	17.9	51.5
Earnings before net changes in fair value of financial instruments				
		42.1	42.4	126.3
(Gain) loss in the fair value of financial instruments		74.4	77.2	65.4
Income tax expense (credit) on changes in the fair value of financial instruments		(20.8)	(23.0)	(17.6)
Net profit (loss)				
		(11.5)	(11.8)	78.5

These statements are to be read in conjunction with the accompanying notes.

Consolidated statement of financial position

As at 30 September 2011

	UNAUDITED	UNAUDITED	AUDITED
	30 SEP 2011	30 SEP 2010	30 JUN 2011
	\$M	\$M	\$M
ASSETS EMPLOYED			
Current assets			
Cash and cash equivalents	2.4	27.6	1.6
Trade and other receivables	74.5	66.5	75.3
Current tax asset	–	–	–
NZPCL investments	–	2.7	–
Other investments	66.5	63.4	65.7
Derivatives and hedge commitment in gain	51.3	40.9	52.4
Non current assets held for sale	37.4	25.4	37.5
Inventories	12.3	12.0	11.7
	244.4	238.5	244.2
Non current assets			
Trade and other receivables	16.8	9.4	16.3
NZPCL investment	112.8	98.2	100.4
Derivatives and hedge commitment in gain	171.2	195.8	167.7
Other financial assets	5.0	3.9	3.9
Property, plant and equipment	2,644.7	2,598.1	2,612.0
Capital work in progress	862.6	424.4	737.2
Intangibles	286.6	161.1	288.9
	4,099.7	3,490.9	3,926.4
TOTAL ASSETS EMPLOYED	4,344.1	3,729.4	4,170.6
FUNDS EMPLOYED			
Current liabilities			
Trade and other payables	97.9	78.0	158.0
Current tax liability	14.3	11.6	5.8
NZPCL debt	–	2.7	–
Current debt	576.2	185.5	493.5
Derivatives and hedge commitment in loss	129.9	103.7	130.9
Deferred income	36.5	33.8	34.8
Provisions	5.4	3.6	13.7
	860.2	418.9	836.7
Non current liabilities			
Non current payables	2.5	2.5	1.7
Finance lease liabilities	1.1	1.3	1.0
Derivatives and hedge commitment in loss	221.9	188.2	214.3
NZPCL debt	123.3	110.0	103.9
Non current debt	1,465.7	1,417.7	1,315.4
Deferred tax	135.3	134.0	155.0
Provisions	12.1	13.6	9.1
	1,961.9	1,867.3	1,800.4
Total liabilities	2,822.1	2,286.2	2,637.1
Equity			
Capital	1,200.0	1,200.0	1,200.0
Available for sale financial assets reserve	(0.9)	(0.9)	(0.9)
Accumulated surplus (deficit)	330.1	252.3	336.6
Non controlling interest	(7.2)	(8.2)	(2.2)
Total equity	1,522.0	1,443.2	1,533.5
TOTAL FUNDS EMPLOYED	4,344.1	3,729.4	4,170.6

These statements are to be read in conjunction with the accompanying notes.

Consolidated cash flow statement

For the three months ended 30 September 2011

	UNAUDITED	UNAUDITED	AUDITED
	3 MONTHS 30 SEP 2011	3 MONTHS 30 SEP 2010	YEAR 30 JUN 2011
	\$M	\$M	\$M
CASH FLOW FROM OPERATIONS			
Cash was provided from:			
Receipts from customers	187.3	177.3	724.6
Interest received	0.1	0.1	5.8
Cash was applied to:			
Payments to suppliers and employees	(94.1)	(85.3)	(292.7)
Tax payments	(6.0)	(3.0)	(27.2)
Interest paid	(35.1)	(27.3)	(125.1)
Net cash inflows from operations	52.2	61.8	285.4
CASH FLOW FROM INVESTMENTS			
Cash was provided from:			
Sale of property, plant and equipment	4.4	2.0	25.4
Short-term investments	64.8	102.8	437.1
Cash was applied to:			
Purchase of property, plant and equipment	(225.1)	(117.0)	(663.7)
Short-term investments	(65.5)	(103.0)	(432.7)
Net cash outflows to investments	(221.4)	(115.2)	(633.9)
CASH FLOW FROM FINANCING			
Cash was provided from:			
Increase in loans	612.3	149.4	1,171.9
Cash was applied to:			
Increase in long-term investments	–	–	–
Dividends paid	–	–	–
Repayment of loans	(442.3)	(91.3)	(844.7)
Net cash inflows from financing	170.0	58.1	327.2
Net increase (decrease) in cash held	0.8	4.7	(21.3)
Opening balance brought forward	1.6	22.9	22.9
Closing net cash carried forward	2.4	27.6	1.6
Closing net cash carried forward comprises:			
Cash and bank	2.4	27.6	1.6

These statements are to be read in conjunction with the accompanying notes.

Notes to the financial statements

For the three months ended 30 September 2011

1. STATEMENT OF ACCOUNTING POLICIES

Reporting entity and statutory base

Transpower New Zealand Limited is a State-Owned Enterprise registered in New Zealand under the Companies Act 1993. The financial statements are in New Zealand dollars and are of Transpower New Zealand Limited and its subsidiaries (Transpower).

Nature of operations

Transpower is the owner and operator of New Zealand's national electricity grid. Transpower is a profit orientated entity for the purposes of NZIAS 1 "Presentation of Financial Statements".

Basis of preparation

The financial statements included in this quarterly report have been prepared in a manner consistent with the financial statements and relevant notes included in the Transpower 2010/11 Annual Report.

The accounting policies used in preparation of these financial statements are consistent with those used in preparation of the Group financial statements for the year ended 30 June 2011.

Transpower's operations are not considered seasonal or cyclical in nature.

New standards not yet adopted

There were no relevant standards issued in the period.

New standards adopted during the period

There were no new or revised standards adopted that had a material impact on the financial statements.

Notes to the financial statements continued

For the three months ended 30 September 2011

2 OPERATING REVENUE	UNAUDITED	UNAUDITED	AUDITED
	3 MONTHS 30 SEP 2011 \$M	3 MONTHS 30 SEP 2010 \$M	YEAR 30 JUN 2011 \$M
Transmission revenue			
HVAC interconnection	124.3	113.5	464.8
HVAC connection	29.9	31.3	124.0
EV (rebate) charge – HVAC	(12.6)	(10.1)	(42.8)
HVDC	21.2	21.2	84.9
New investment agreements	6.9	6.6	26.6
Other	3.6	1.6	17.8
	173.3	164.1	675.3
Other revenue			
System Operator	8.4	7.7	31.4
Rental income	2.0	2.0	8.0
Risk Reinsurance investment income	0.7	0.7	2.9
Other	2.8	4.1	13.8
	13.9	14.5	56.1
Total operating revenue (excluding finance revenue)	187.2	178.6	731.4

Transmission revenue

Transmission revenue consists of charges for the transmission of electricity from the point of generation to the point of supply, being high voltage alternating current (HVAC) interconnection, connection and high voltage direct current (HVDC).

Transpower operates its revenue setting methodology within an Economic Value (“EV”) framework that analyses economic gains and losses between those attributable to shareholders and those attributable to customers. The balance of the accumulated gain (loss) from regulated transmission activities attributable to customers (“the EV balance”) is passed on to or claimed from customers over time as EV rebates or charges.

New investment agreements, or customer investment contracts, are contracts entered into with customers to build grid connection assets.

Other revenue*System Operator*

System Operator income relates to payments received for the provision of real time services to ensure the short-term security of the New Zealand electricity system.

Other

Other revenue mainly consists of subsidiary income from d-cyphaTrade Limited.

Notes to the financial statements continued

For the three months ended 30 September 2011

3. OPERATING EXPENSES	UNAUDITED	UNAUDITED	AUDITED
	3 MONTHS 30 SEP 2011 \$M	3 MONTHS 30 SEP 2010 \$M	YEAR 30 JUN 2011 \$M
Transmission expenses			
Maintenance of HVAC substations	12.1	11.5	52.1
Maintenance of HVDC substations and cables	2.7	1.9	11.1
Maintenance of HVAC lines	7.3	8.3	46.4
Maintenance of HVDC lines	0.1	0.3	1.3
HVDC share of reserves	0.4	1.1	4.7
Other direct transmission expenses	6.3	5.8	25.4
	28.9	28.9	141.0
Employee benefits			
Short term benefits	13.9	13.0	52.6
Defined contribution schemes	0.9	0.8	2.6
Other	–	–	1.2
	14.8	13.8	56.4
Other operating expenditure			
Information technology costs	5.1	4.5	19.5
Industry levies	2.0	2.4	7.0
Other business support costs	9.0	7.8	34.5
Operating lease and rental costs	4.4	3.7	15.8
External auditor – audit fee	0.1	0.1	0.3
External auditor – other assurance	–	–	0.3
Insurance	1.0	1.0	4.4
	21.6	19.5	81.8
Total operating expenses	65.3	62.2	279.2

Maintenance includes inspection, servicing and repair costs.

Other direct transmission expenditure includes investigations work that the Group conducts (prior to any commencement of a capital project) and the costs associated with running the Group's communications network.

Information technology costs include such items as software licences, maintenance, application support and project investigations.

Other business support costs include such items as legal fees, office equipment, communications, vehicles, travel consultants, donations and study grants.

Notes to the financial statements continued

For the three months ended 30 September 2011

4 NET FINANCE EXPENSES

	UNAUDITED	UNAUDITED	AUDITED
	3 MONTHS 30 SEP 2011	3 MONTHS 30 SEP 2010	YEAR 30 JUN 2011
	\$M	\$M	\$M
Finance revenue			
Interest received	0.1	0.1	5.8
Finance expenses			
Interest paid and associated fees	34.5	26.6	122.0
Cross border lease expenses	–	0.1	0.7
Capitalised interest	(14.3)	(7.7)	(37.8)
Imputed interest	0.6	0.6	2.4
	20.8	19.6	87.3
Total net finance expenses	20.7	19.5	81.5

Interest paid and associated fees

All interest paid is on financial instruments designated as fair value through profit or loss.

Imputed interest

Imputed interest is on new investment agreements, transmission realignment and certain other prepaid transactions.

SCI performance targets

FINANCIAL PERFORMANCE TARGETS	3 MONTHS 30 SEP 2011	FULL YEAR TARGET
EBITDAIF ¹ margin	65.1%	63.2%
Funds from operations interest coverage	3.0	2.8
Return on capital employed ²	7.8%	7.3%
Return on equity ²	10.2%	9.9%
Average total transmission costs (c/kWh) ²	1.78	1.75
Estimated economic value added (\$m)	(3)	(13)

NON-FINANCIAL PERFORMANCE TARGETS	3 MONTHS 30 SEP 2011	FULL YEAR TARGET
Material breaches of system operator performance obligations reported to the Electricity Authority	0	<4
ACC workplace safety audit status	Tertiary	Tertiary
Number of fatalities or injuries causing permanent disabilities	0	0
Number of medical treatment injuries	15	<26

OPERATIONAL PERFORMANCE TARGETS	3 MONTHS 30 SEP 2011	FULL YEAR TARGET
High voltage alternating current (HVAC) circuit availability	99.3%	98.5%
High voltage direct current (HVDC) (pole 2 only) availability	79.7% ³	82.5%
Number of loss of supply events of greater than 0.05 system minutes	3.0	21
Number of loss of supply events of greater than 1.0 system minute	1.0	3.0

¹ EARNINGS BEFORE INTEREST EXPENSE, TAX, DEPRECIATION, AMORTISATION, IMPAIRMENT AND CHANGES IN THE FAIR VALUE OF FINANCIAL INSTRUMENTS.

² THE YEAR TO DATE RESULTS HAVE BEEN ANNUALISED.

³ POLE 2 AVAILABILITY HAS BEEN MUCH REDUCED FROM MARCH TO AUGUST BECAUSE IT WAS BEING OPERATED AT REDUCED CAPACITY DURING RE-CONDUCTORING OF THE NORTH ISLAND SECTION OF THE HVDC LINE.

