Annual Results Briefing 15 August 2007

<u>Simon Mackenzie Commentary</u>

Agenda (Slide 2)

Thanks Michael.

I think it's fair to say that Vector has had another eventful year and personally, the three weeks I have been in the CEO's chair have been no less eventful.

Today I'll talk first about the four key health indicators for Vector and then discuss my vision for Vector's next phase as well as important regulatory issues in front of us.

Chris will talk about our financial performance in more detail and, after that, we will be open for questions.

In the interests of time, we won't be going into the finer details of the operations results. As previously, the detail is in the supporting information pack you have been given, but if you have any questions of course we'd be pleased to answer them.

Health Chart

Slide 3

1. Earnings

We have recorded net earnings of $101.7 million for the year ended 30 June 2007. As announced to the market on 30 July, this includes a one-off gain of $40 million as a result of the change in Vector's deferred tax liability.

This, in turn, is the result of the reduction in the corporate tax rate from 33% to 30% enacted in May and to take effect from 1 July next year. It required us to restate our deferred tax liabilities at the lower rate as part of our year-end accounting processes.

The deferred tax adjustment is a non-recurring item and, as a non-cash accounting entry, has no impact on our underlying profitability and cash flows, and therefore our dividend payment.

Excluding this item, net earnings from underlying business increased by a very pleasing 36.9% to $61.7 million. This is at the upper end of the $58 million to $63 million guidance we gave to the market in May.

Vector is reporting a strong performance by all of its core businesses, with each making increased earnings contribution to the year's result.

A substantial 19.4% increase in operating revenue reflects volume and connection growth on our infrastructure networks, higher energy use as a result of the return to more seasonable winter weather following the warmer winter of 2005, and higher natural gas sales including one-off contracts.

However, operating expenditure also increased significantly, due to additional gas purchases required to meet increased demand from new and existing gas customers, rates on our infrastructure networks, and increased regulatory compliance costs.

This, combined with tighter margins, restricted our EBITDA increase to 5.4%. The margin pressure is identifiable in the gas business, where our weighted costs are increasing as we continue to transition off Maui legacy entitlements. I will talk later about changes in the gas sector.

Net profit after tax and before amortisation - (NPATA) - of $199.9 million also incorporates the $40 million deferred tax adjustment. Vector's dividend policy is effectively linked to NPATA, but this $40 million one-off accounting adjustment is not included in our dividend considerations.

Chris will give you more detail on the financial result shortly.

Turning to our core business areas I will discuss their performance as well as our on-going focus going forward.

Slide 4

Photos of Storm Response

But first off, I'd like to talk about a recent event which although outside the reporting period reminds us of the impact Vector has on customers' daily lives – the storm and associated outages in July. For me this is always a reality check. The storm was four days old when I was put in the hot seat – in the CEO's chair and facing Mark Sainsbury on national television.

However, the July hurricane – yes the winds were hurricane force - was, without doubt, a major test of our capabilities and the patience and endurance of our customers.

Vector acknowledges the inconvenience and disruption experienced by customers who were without power for extended periods. The extent of the damage was such that a group of customers were without power for days and we know this was difficult and trying for them.

Here are some key facts which paint the picture and again the stark reality of what we were dealing with:

- Winds of up to 180km per hour and a storm which MetService tells us was worse than the weather bomb and worse than Cyclone Bola
- At the peak we had 150,000 customers off and within 24hours 100,000 back on

- Over the week around 500 field crew worked 24/7 to restore power for customers

- Nine helicopters were used to survey damage and dispatch crews

- Around 80% of the damage was caused by falling trees and this is in spite of the fact we trimmed around 100,000 trees last year – most by the way, requiring individual resource consents.

For the record, I am very proud of the dedication shown by our staff and field service partners who worked tirelessly for long hours in round-the-clock shifts to restore power supplies.

As I said publicly at the time we have instigated a review of our response and the initial findings were presented to the board yesterday. The key conclusion is that we need to improve how we communicate directly and through the retailers with our customers, providing them up to date information on their specific faults. We are taking steps to remedy this, some short term and some long terms solutions. Ultimately the strength of our communications to our customers and the performance of our network during such events is the key determinant of how our brand and our people are judged. My commitment is that we build the capacity to protect all three – customers, staff and brand.

Turning now to the past year's results. Slide 5

3. Electricity Network Throughput

Electricity business revenue grew from $580.1 million in the 06 year to $611.5 million in '07, an increase of 5.4%. The lower left graph shows a **1.9%** lift in total electricity network throughput. This is due in part to the return to more normal winter temperatures, but also reflects the addition of over 10,000 new connections to our networks and higher per-customer electricity usage, particularly in Wellington. Over 80% of the new connections occurred on our more extensive Auckland networks. *(Simon: 8,291 of the total 10,172 new connections – or 81.5% - on greater Auckland network).*

4. SAIDI

The SAIDI measure of electricity network availability as it impacts our customers, at the top right shows both the outcome for the regulatory year to 31 March 2007, and the first quarter of the new regulatory year to 30 June.

As previously reported in our third quarter report in May, we completed the regulatory year with supply interruptions arising from normal operations slightly below the 85.5 minutes SAIDI regulatory threshold for supply quality.

We recorded 83.8 SAIDI minutes arising from normal operations, and a further 31.8 minutes attributable to extreme events, which include severe storms, using our extreme event assessment methodology. I note that formally defining an extreme event is something the Commerce Commission has still to finalise.

5. Gas Business and Throughput

Revenue grew by 37.5% to $668.2 million attributable to one-off higher natural gas and strong LPG sales. These were a result of demand growth and one-off supply contracts which were key contributors to a strong result by this business.

Turning now to gas throughput, gas shipped through our transmission system is around **11 petajoules down** on the previous year. That isn't surprising as transmission throughput during 2005/06 year was unusually high due to the increased demand for thermal power generation at a time of constrained hydro resources.

Throughput differences associated with deliveries to power stations have little impact on transmission revenues as gas for these customers is transported under fixed contract arrangements.

Distribution network volumes for the year were 3.5% lower at **22 petajoules** due mainly to the loss of two large wood processing customers which offset volume gains from increased gas consumption following the warmer 2005 winter and a net gain of just over **4,000** new connections – most of them (64%) on our Auckland gas network.

The new connections included over **430** higher load commercial businesses.

Efficiency improvements at our gas treatment plant at Kapuni have seen the plant's uptime increase from 96% last year to 99.5%, with an associated saving of about $1.6 million.

6. Technology

The technology business, incorporating energy metering and telecommunications, delivered a solid combined performance with EBITDA up by 12.7%. While this part of our business is smaller by measure of financial contribution, it is strategically significant. I will outline why I believe this.

Firstly, I'd like to talk about metering.

Energy metering technology internationally is transitioning rapidly from simple meters to technologically advanced meters that offer customers real time information to help monitor and manage their energy use.

You will recall Vector is partnering with the international arm of Siemens to strengthen our capabilities in the energy services field. The partnership will combine Siemens' global technological and operational expertise in metering services with Vector's strong team and expertise in the local market.

My focus is on finalising contractual arrangements with Siemens so we can move forward to deliver smart metering solutions for New Zealand. We need to get on with business and this is a key priority. I am confident the partnership brings together the right mix of capabilities, technology and experience to truly make an impact on the metering landscape.

SLIDE 6 – picture of launch

Telecommunications – you'll see a photo here taken at the launch of the first Vector connected school on the North Shore earlier this year.

Not a day goes by where broadband and related issues are not providing the media with new, usually dire, stories of New Zealand's offerings.

The contribution true broadband can make to economies is acknowledged globally and Vector is pleased to play its part for New Zealand. The question we get asked often is exactly what is that part and where exactly might we play in the future.

The answer is this – Vector Communications is a valuable asset for us with its existing fibre but importantly we have a number of other highly valuable assets and capabilities that put us in a unique position that we could leverage. There has been a lot of speculation about our plans in telecommunications and can I re-iterate that no decision has been made. However, where we take this business in the future is a major work stream for us and we are seriously focused on exploring if the environment is right for Vector to deliver the true broadband New Zealand is asking for. Let's face it – the needs of customers and the economy are great and those with the ability to step up, extremely limited. Vector has that ability but that must be matched by the right partnerships, incentives, return on investment and regulatory environment.

Evidence of what we can achieve is the rollout of fibre optic cable on the North Shore under the Government's Broadband Challenge.

Under the successful joint bid with North Shore City Council we provide true broadband services to over 40 schools, six libraries and 15 council facilities in North Shore City. These groups are now enjoying all the benefits true broadband offers and in turn highlights the huge gap between old and new. Excuse the pun but the difference, is light years apart…

We will also continue our on-going interface with regulators and Ministers and we will of course keep the market appropriately informed of any decisions.

Slide 7

Regulation

It will come as no surprise that we are currently managing a very full regulatory agenda, with over 50 regulatory, industry governance and policy development initiatives under active management.

When looking back on the year it is pleasing to report that we have a significantly strengthened relationship at the regulatory level and we continue to engage constructively with key ministers, other Members of Parliament and officials.

I'd now like to touch on some of the more significant matters occupying our attention.

Slide 8

Commerce Act Review

This above all else will define our future. We welcomed the announcement by the Minister of Commerce of the review of Parts 4, 4A and 5 of the Commerce Act, which is the regulatory framework for infrastructure assets such as ours. The principle objective being to ensure that the regulatory framework delivers certainty and confidence thereby enabling investment.

Of course this must strike the right balance between incentives for investment and consumer protection.

The key components to achieve these objectives are:

- Input methodologies
- Merits review
- Greater options for regulatory frameworks
- Market tests.

The options for regulatory terms include:

- Negotiate/arbitrate
- Thresholds regime
- Propose and respond
- Information disclosure.

Together these provide a broader framework which ultimately will lead to more robust regulatory outcomes.

From our point of view the process to date has been constructive and inclusive with government, industry and expert advisors working well together.

I'd like to again acknowledge the role that the Government policy statement in August last year played in setting the context for the Commerce Act review. That policy statement still gives us encouragement from a future investment perspective.

Administrative Settlement

As you know our settlement offer was agreed in principle with the Commerce Commission in October last year and final resolution awaits the Commission's reasons document and subsequent public consultation process. Latest advice from the Commission is that this is due to happen in September with a decision soon after. We look forward to the conclusion of this matter.

In the meantime, we are performing consistently with the terms of the in-principle agreement, including our undertakings to continue with the voluntary rebalancing programme across customer groups and network regions. We continue to invest in our networks to an appropriate level to ensure safety and security of supply.

Electricity Thresholds Reset in 2009

The price and quality thresholds regime for electricity lines companies, including Vector, is due to expire on 31 March 2009. The Commerce Commission has initiated a process to reset the thresholds, and Vector is working constructively to provide information to the Commission to support its analysis.

The Commission has not yet communicated the terms of the reset or the methods that will apply. However we are working through the issues with the Commission to ensure increasing demands for quality infrastructure are balanced with the needs of shareholders for commercially appropriate returns.

Our discussions with the Commission on this issue demonstrate to us the Commission's recognition of the importance of this balance and the impact it has on business and consumers.

There is a possibility that the reset process may be superseded by new regulatory control provisions arising from the Commerce Act review.

Slide 9

Gas Control Final Authorisation

On control of our Auckland gas networks, we continue to operate under the provisional authorisation. We have been working with the Commission to provide information so a decision can be made on the terms of a final authorisation.

Review of Electricity Industry Reform Act

Changes being flagged in the third review of the Electricity Industry Reform Act since 2001 are consistent with Government policy objectives to encourage investment in infrastructure, particularly renewable generation.

We believe the proposed changes are in the right direction and see a relaxation of the governance rules around lines companies' involvement in generation as an opportunity for companies like ours to explore options.

Our main concern is around the extent to which the legislation assumes line companies are able to take advantage of their natural monopoly position, as we believe this is adequately addressed in existing competition legislation.

Industry Issues slide 10

Electricity Commission

We continue our strong relationship with the Electricity Commission working with them on a number of fronts.

Our core focus remains in transmission investment, transmission pricing methodology and the delivery of both in a timely manner. To us, this feeds directly into security of supply, an issue that must constantly be top of mind.

Security of Supply

On security of supply, we welcome the Electricity Commission's approval last month of Transpower's new transmission line between south Waikato and south Auckland. This will certainly help to improve security of supply to not just Auckland but the whole of the upper North Island.

Following the Transpower outages last June the Minister of Energy indicated to Vector the importance he places on seeing security of supply issues resolved. We have been working constructively with Transpower on a number of initiatives.

Over the past nine months we have been working with Transpower to determine how they can utilise some of our assets – such as the Auckland tunnel – to strengthen supply into Auckland. This work continues and recognising the significant value of our assets we are hopeful an appropriate commercial arrangement can be reached shortly.

In addition, Transpower and Vector jointly commissioned a review of supply into Auckland by the international consulting arm of Siemens AG. This report is on Transpower's website. It raises some key issues that we take a strong interest in. Again this relates to security of supply and our obvious commitment to our customers plus our own confidence.

On the gas transmission side, increased energy consumption has led to the need for further generation and we continue to work on enabling this through transmission upgrades for example.

EECA

Another important agency that we work closely with is EECA – the Energy Efficiency and Conservation Authority. EECA has a central role going forward in driving many energy efficiency initiatives that align with Government objectives.

Slide 11

Climate Change Policy and New Zealand Energy Strategy

Similar to broadband, not a day goes by where you don't read or hear something relating to climate change. The signs are all there – that this is the start of a revolution – not just evolution – for all New Zealand consumers including the energy sector. Therefore it is only right that Vector considers its place in the future world.

My vision is for Vector is to be the lead provider and innovator of demand side solutions which put energy choices back in the hands of the customer. Perhaps it is not 'back' in the customers' hands as arguably energy choices were never theirs to make.

We have the ideal platform to offer the best of what we currently have – given our core infrastructure assets and supplement this with new innovations to provide a suite of customer led energy solutions.

What I mean by platform is our combined asset mix - electricity, gas plus technology – metering and telecommunications.

To lead this space we are pursuing options to add other solutions in the mix. My focus is to re-orientate the current paradigm to one that offers customers options and choice.

Slide 12

As you will know we have taken some small, but important steps in the form of the NZ Windfarms shareholding and the trial of micro-wind turbines.

I was not surprised at the level of significant customer response we had following the launch of the micro wind trial. Individual consumers, business, developers, builders and even schools approached us about how they could get a turbine. This was irrespective of the fact we made it clear we are in trial mode only and that prices are not at a level we would expect consumers to bear. Well we got that point wrong!

Like I said these are small steps and you could argue miniscule parts of our business. We know that but we also know the wave of consumer demand has only begun to build. We also know that not listening to customers, not taking in what is going on around us would be just plain dumb. Bluntly we have to position ourselves to the changing consumer, global and political climate. It is a climate of change so expect us to keep listening, and evolving.

Slide 13

Vector's next phase

The burning question is perhaps not where we have been but where are we headed.

Yes I have only been in this role for 21 days but I have been in the business for some time and what is absolutely apparent is we have some hard work to do. My immediate focus is in two parts – the first to drive our strategic options and equally importantly to lead the business on a cost efficiency programme which will maximise our performance and get us to the place I believe we should be.

We have already got started and made some initial reductions as well as developing a structured plan to get us there. We must maximise efficiencies and manage costs effectively to ensure on going shareholder value creation.

This forms one of four key focus areas for Vector over the coming year. Every initiative and decision will be driven by these four key considerations:

- To reiterate – a cost efficiency programme. I have a priority focus on cost management across the business – both capital expenditure and operating expenditure.
- Regulatory and customer outcomes - how does the prevailing or anticipated regulatory environment impact on customers, assets or initiative? I can't overstate the importance to our future strategic development of regulatory

outcomes. We must also be constantly aware that for our business strategy, performance and regulation go hand in hand.

- Will it achieve our operational excellence and core business enhancement objectives? This includes how we can do things smarter and how do we leverage our current business combined with the new and innovative packages to offer customers that they will increasingly demand in this changing environment.
- And, where we are contemplating growth initiatives, they must meet the disciplines of strategic alignment, return on investment and risk.

And finally to summarise earlier points in the context of Vector's next phase.

As I mentioned earlier an accelerated work programme is currently underway to examine what part Vector can play in delivering to the country's broadband needs.

We continue to look for growth in our core businesses. We will review our current asset mix and look at options to change our portfolio where there is value.

We will take a lead role in developing demand side solutions for customers, acknowledging climate change as a key driver for a new approach to energy.

You can expect our focus on customers to increase over the next year. They have every right to expect a lot from us.

As do our shareholders – they have every right to expect a lot from us. To loop back, our focus on cost efficiency and growth is critical to ensure we deliver to all of these expectations.

I hope that provides some insight into my thinking and where we see Vector heading as we enter a new phase.

Thanks for your time and I'll now hand over to Chris.