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Contact's strategic initiatives position it well for the future

2010 financial year in review

The financial year ended 30 June 2010 was not without its challenges with the impacts of portfolio inflexibility in another wet year hindering Contact's performance. However Contact's Managing Director, David Baldwin, said the company has made significant progress in the projects it initiated in 2007 to restore portfolio flexibility, which are expected to be complete later this year.

Contact reported today underlying earnings after tax for the year of \$150 million down 6 per cent from \$159 million. Earnings Before Net Interest Expense, Taxation, Depreciation Amortisation, Change in Fair Value of Financial Instruments and Other Significant Items (EBITDAF) were \$427 million, down 4 per cent from \$445 million in the 2009 financial year.

Mr Baldwin said the wet conditions during the 2010 financial year came at a time when Contact was contractually obligated to pay for gas that it was unable to use in its gas-fired power stations, because of the amount of hydro generation available.

"I'm immensely proud of how the Contact team responded to the gas challenges during the year. Their efforts to accelerate the development of the Ahuroa gas storage project resulted in the injection of about 10 per cent of Contact's gas requirements during the year, saving the company tens of millions of dollars.

"It shows how important the Ahuroa gas storage project is to Contact in re-establishing gas supply flexibility – and the gains that are possible by the company being able to turn off its gas-fired power stations and store the gas for use when it is most required."

Retail competition continued to intensify during the year with the number of customers switching retailers increasing from an average of 20,000 per month in July 2009 to around 25,000 per month in July 2010. Mr Baldwin said that Contact had largely maintained its customer numbers over the year, in spite of the increasing competition.

"The retail team performed strongly during the year in so many ways, particularly in the way they engaged with customers. The seven per cent increase in sales volume to commercial and industrial (time-of-use) customers was also a great result, given the competitiveness of the market."

Contact also made significant progress in a number of other key areas during the financial year.

At the half year, Contact reported that construction of the company's \$100 million, 23 megawatt Tauhara 1 geothermal plant was on track, with commissioning of the plant expected around mid 2010. "Contact's geothermal development team did an outstanding

job in delivering – what is now known as the Te Huka power plant – into commercial operation on 23 May, under budget and ahead of schedule,” said Mr Baldwin.

Acknowledging another major accomplishment over the 2010 financial year, Mr Baldwin said that Taheke 8C and the Adjoining Blocks Incorporation had selected Contact to be its joint development partner for the Taheke geothermal project. “This is very exciting for Contact as it’s the first step in establishing partnerships with iwi to develop new geothermal resources.

“We’re thrilled to be partnering with Taheke 8C and are looking forward to commencing exploration drilling within the next few weeks,” he said.

The construction of Contact’s \$250 million gas-fired peaking project also made good progress. The project is currently being commissioned and is expected to be fully operational in late 2010. When completed, the new power station will provide a source of flexible generation for times when weather-dependent renewables are unable to meet demand, or when other power stations are undergoing maintenance.

The company is continuing to develop its Te Mihi geothermal power station (having obtained final resource consents in 2008) and is presently consenting Contact’s proposed Tauhara 2 power station – a geothermal plant of up to 250 megawatts. A key step for Tauhara 2 occurred with the submission of the application to the Environment Protection Authority and the scheduling of the hearing which will provide certainty of decision on the project early in 2011.

Well positioned for growth

Contact’s strategy for growth remains focussed on pursuing a range of options across the major fuel types – thermal, geothermal, wind and hydro – that the company can execute at the right time to suit the changing operating environment.

In addition to the array of geothermal projects the company is currently developing, Contact is also continuing to advance resource consent applications for its proposed Hauauru ma raki (HMR) and Waitahora wind farm projects (located in north-west Waikato, and the northern Wairarapa respectively). Also, Contact is continuing to engage with community groups on potential future hydro projects on the Clutha River, in addition to investigating several North Island sites for new gas-fired generation projects.

People

Mr Baldwin said he was pleased with the progress in the company’s safety performance, reducing its total recordable injury frequency rate by 25 per cent over the year. “I said last year that a key priority was to foster the company’s safety culture in order to progress toward our aspiration of zero harm. The organisation has made great progress and the goals we’ve set for ourselves for the year ahead will take us another step closer toward our aspiration.”

He also said that the strength of the company continued to be reflected in the calibre of the people it was able to retain and attract - Dean Stebbing joined Contact this month in a role entitled Kaawai Rautaki (Strategic Partnerships).

“This is a new role in Contact and represents a step forward for the company as we explore our potential to grow our generation assets, including in partnership with iwi.

Dean will be responsible for helping us build our strategic partnerships with iwi and related parties and will be working across all aspects of the business,” said Mr Baldwin.

Distribution to shareholders

The Contact board of directors resolved that the final distribution to shareholders would be the equivalent of 14 cents per share resulting in a total distribution of 25 cents per share, a reduction of 3 cents from the prior financial year. The 2010 distribution to shareholders reflects the financial performance of the year in review, which was impacted primarily by wet conditions. The possibility that the distribution might be adjusted if hydrology (among other things) continued to impact Contact’s performance in the near-to-medium term was signalled in August 2009 and February 2010. The distribution represents a payout ratio of 100% of Contact’s underlying earnings per share.

Outlook

In light of the range of market and operating uncertainties, particularly in relation to hydrology, it would be inappropriate to provide specific quantitative guidance for the 2011 full-year performance. Commenting on the key drivers of performance, Mr Baldwin said: “The 2011 financial year will be a year of two halves. Continuing high levels of take-or-pay gas and high hydro inflows will likely result in the first half being broadly similar to the first half of the 2010 financial year. EBITDAF in the second half of the 2011 financial year is expected to benefit from increased operational flexibility as the Ahuroa gas storage and Stratford peaker plant are brought into commercial operation, and as take-or-pay gas levels reduce from January 2011.

Mr Baldwin said with the portfolio well on its way to restoring flexibility, geothermal development will become Contact’s priority generation investment.

“Investment in base load generation as well as flexible assets such as peakers and gas storage will help to alleviate the future demands put on the country’s energy supply. Whereas New Zealand was formerly seen as “energy-constrained”, it is now both energy and capacity constrained. Contact’s strategy seeks to address both of these issues.

“I am looking forward to a series of major milestones being achieved over the next 12 months with the Stratford peakers and the gas storage reaching commercial operation, and the outcomes of the consent processes for our new geothermal, wind and gas generation developments. These initiatives underpin Contact’s future growth for the next decade and security of supply for the country,” said Mr Baldwin.

Media enquiries

Janet Carson
021 242 5723

Investor enquiries

Liz Kelly
021 461 302