CONNECTING WITH OUR CUSTOMERS

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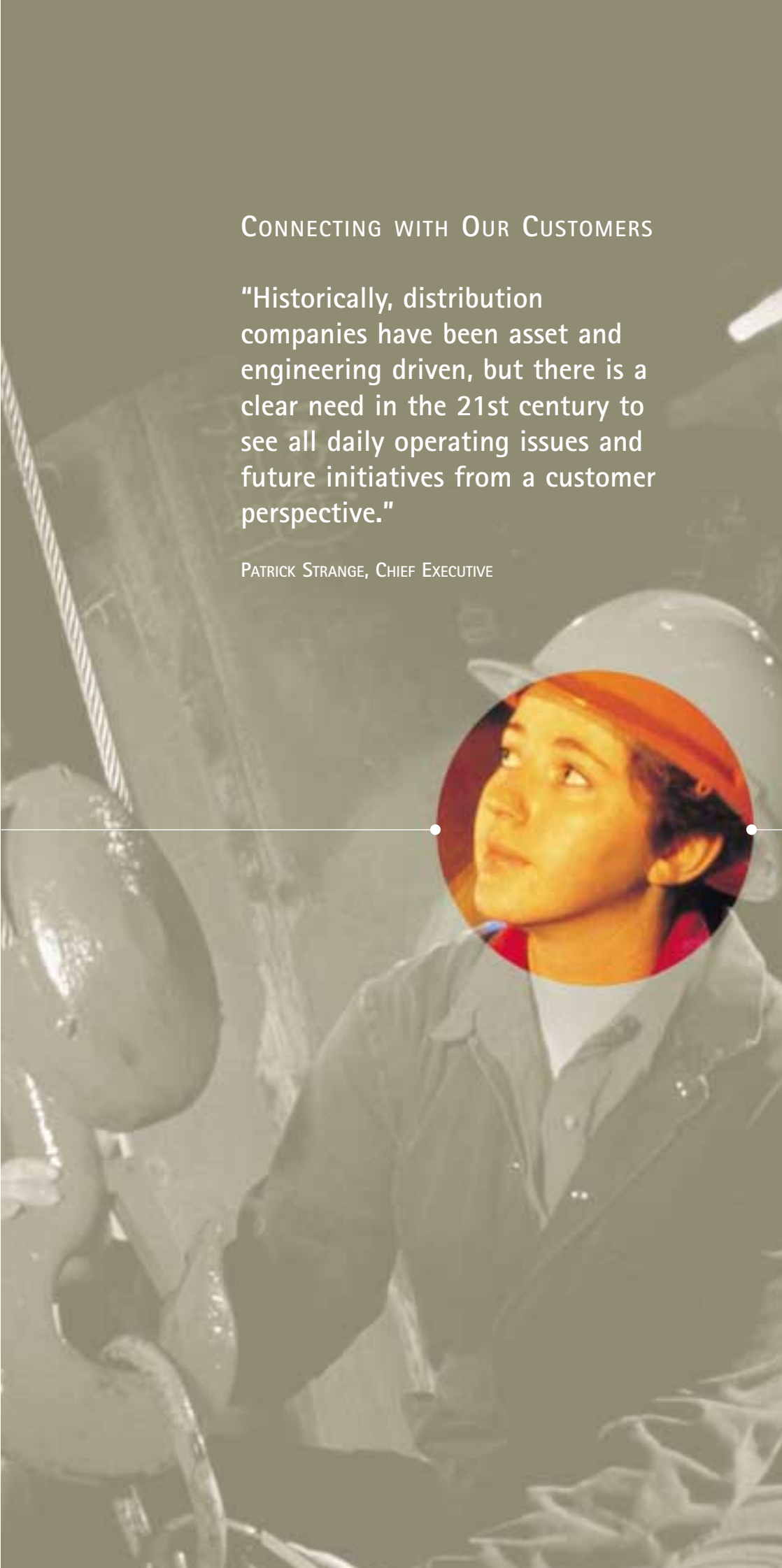
Connecting with Our Customers

"Historically, distribution companies have been asset and engineering driven, but there is a clear need in the 21st century to see all daily operating issues and future initiatives from a customer perspective."

Patrick Strange, Chief Executive



Facts about Vector

- VECTOR is an infrastructure operator, focused on its core business of electricity distribution. It also owns a fibre optic cabling network, providing connections to Auckland businesses
- VECTOR is the second largest electricity distribution business in New Zealand
- The company's service territory is the fastest growing of all network businesses in New Zealand
- The company has nearly 270,000 customers and over $1 billion in assets
- VECTOR has a total of 8,711 kilometres of sub-transmission cables and distribution lines
- The company obtains its bulk supply of electricity from the national grid, Transpower, and is the only New Zealand network to use 110 kV high-voltage cable in its system
- One hundred per cent of its subtransmission and 63 per cent of the distribution system is underground, a relatively high proportion by national standards.

vector

2001 Annual Report

Highlights

- Net profit after tax of $72 million
- Dividend of $48 million
- 40 year overhead improvement and undergrounding programme established
- Record low customer disruption figures
- Further reduced operating cost per customer
- Completion of largest-ever capital works project
- Diversification to utilise fibre optic cabling network

"VECTOR operates with a conservative balance sheet and is in a very strong financial position."

Chairman's Report The Power to Build

VECTOR has successfully completed a year focused on a continued search for higher levels of reliability, quality of supply and customer service. Milestones included record low customer interruption figures, completion of our largest ever capital works programme culminating in livening of the tunnel cables, and the start up of Tangent, our wholly owned high bandwidth telecommunication company using our fibre optic network.

While the company still has further to go to reach optimal results, it can now go forward from a much sounder base.

Financially, the past year has seen VECTOR advance significantly. The company achieved solid profitability off a very strong balance sheet.

This has been recognised by improved credit ratings from Standard & Poor's, which in December, 2000 re-rated the company's financial status long-term to AA- with stable outlook, a very satisfying improvement from the A+ rating of 1998.

Operating Result

VECTOR attained another solid result, recording a net profit after tax of $72 million for the year ended 31 March, 2001. This is ahead of target, and although a 23 per cent decrease on the previous year, the change is due entirely to higher one-off, non-recurring items that year. The operating surplus before income tax was $98 million, compared with $112 million the previous year.

The core electricity lines business contribution to operating profit increased, as costs continued to reduce. This reduction has been achieved over a period in which the company's system reliability and service has been lifted, and prices have fallen in real terms.

One-off items continued to lift profits in 2001. Future net profit expectations are likely to be closer to $50 million as a result.

Total revenue was $229 million, an increase of $9 million for the continuing lines business. The growth in large part came from new connections. The previous year's revenue, $313 million, included revenue from now divested generation assets.

Financial Position

VECTOR operates with a conservative balance sheet and is in a very strong financial position. The company is low-geared compared to similar businesses with debt at 16 per cent. This is considered prudent as the company is not able to access capital markets in the same way that listed companies can.

Group total assets at the end of March 2001 stood at $1,009 million, up from $985 million at the end of the previous year. The valuation of the network has been updated and stands at $881 million.

The company's revenue base remains well-diversified, with nearly 40 per cent of the energy distributed going to residential customers, and the remainder to a mix of commercial and industrial users. The company has one of the highest customer-density figures in New Zealand and the customer base is growing as Auckland expands. Network-wide, the average growth in new connections is 2 per cent: however, in some areas it is as high as 7 per cent, reflecting both urban infill and urban sprawl.

There will be ongoing capital requirements to meet this growth, and to reinforce and renew the existing network, elements of which are now over 70 years old. However, the company is very well positioned to deal with this.

The Network

VECTOR has now completed the Inner Auckland power supply upgrade programme. While the main focus of this project has been the Central Business District and surrounding inner suburbs, there will be wider benefits, through better

back-up and load-spreading. These benefits include support for northern North Island transmission grid security.
The key Penrose to CBD supply tunnel was commissioned late in the year. This enables the last visible vestiges of the 1998 CBD power crisis, the temporary overhead link from the national grid, to be dismantled.
Inner Auckland now has a power supply that is equal to if not better than most major international cities.
This project is the largest element of a major capital reinvestment programme directed at the network's transmission and subtransmission system over the last three years. Coming over 20 years after the last significant investment, it places VECTOR in good stead for the new century.

Customer Service

Our relationship to our customers is vital. VECTOR has been concerned that the interposed model adopted elsewhere, where all customer interface is via a number of electricity retailers, is not the most effective long-term arrangement for the customer. The extensive problems experienced with retail customer interface following the 1998 Electricity Industry Reform Act in New Zealand gives substance to this concern. VECTOR has thus set itself apart from most lines businesses by retaining contracts with and direct accountability for service to its nearly 270,000 customers. To enhance this, VECTOR is now implementing a system that will link all of its customer information and service activities, so that it can rapidly and efficiently respond to customer inquiries and needs.
The Board takes particular note of the dramatic improvement in VECTOR's reliability and health and safety performance in the last two years, and commends VECTOR and contractor frontline teams for this achievement. But there is still more to be done, and we will set strategies for continuous improvement.

Company Advancement

VECTOR last year established a subsidiary, Tangent, to create value for our shareholders and customers using our existing state of the art communication network. In recent years, VECTOR has installed ducting along with power cables. Fibre optic capacity is now being interconnected and incorporated into an augmented network providing for the next generation needs of customers. Tangent is leading New Zealand electricity distribution companies in this field, and has established itself as a telecommunications network provider in Auckland with an expanding base of high-use customers.
The Board has also agreed with the shareholder, the Auckland Energy Consumer Trust (AECT), to establish a 40 year programme for our existing overhead distribution lines, a major part of which will be undergrounding. Approximately $10 million will be allocated this year towards funding this programme.

Dividends

The company pays an annual dividend each year to the AECT, subject to operating and investment requirements. The Trust then decides how this will be distributed to customers.
In line with this policy, a dividend of $48 million will be paid to the Trust for the financial year ended March 2001.

Governance

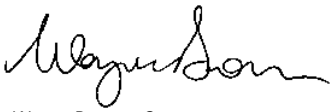
Following AECT elections late last year, a largely new trust is now in place. The board and senior management have conducted initial briefings with new trustees, and I am pleased to report that a sound rapport is developing.
The company is monitoring the Government's response to last year's inquiry into the electricity industry. We do not expect to be adversely impacted financially by the consequent regulatory environment, but the Directors remain concerned that the gains companies such as VECTOR have achieved in customer service are not undermined.
Following the successful closure of outstanding legal actions over the past year, litigation involving the company is at its lowest level for a decade. This included settlement of a long-running dispute with Transpower, and the close co-operation which has emerged between the two companies is very pleasing.

The Community

The company completed a year with another clean record on environmental compliance, reflecting continued focus on proactive environmental management.

Contributions

The Board wishes to thank VECTOR's senior management, staff and contractors for their achievements this year. In particular, congratulations are due for the successful commissioning of the Inner Auckland reinforcement project, which was of a size and complexity never before faced by a New Zealand distribution network.
VECTOR has a well balanced board of experienced directors well suited to the needs of the company. Directors' skills cover the fields of electrical engineering, civil and telecommunication engineering, finance, law and infrastructure management.
I would like to acknowledge the contributions of John Wells (Bancorp Chairman), who chaired the Audit Committee, Doug Dell (a very experienced electrical engineer), who chaired the Risk Management Committee, and John Lindsay and Peter Drummond (both experienced infrastructure managers and directors), whose contributions complimented my own experience in civil engineering and business development.



Wayne Brown, Chairman

Taking the Drama Out of Middlemore

Talk about Middlemore Hospital today and more than likely images from the New Zealand reality television series of the same name are evoked.

Unlike the globally-viewed series "ER", Middlemore was real-life drama, filmed as it happened. The stars were ordinary doctors and nurses.

It opened New Zealanders' eyes to what really goes on in the emergency rooms and operating theatres as accident victims are wheeled in. It also highlighted the vital importance of avoiding delays and setbacks.

Power supply failure at critical moments is clearly a danger emergency room doctors don't need. In the first instance, they can usually rely on an emergency generator to cut in – but this is not fail-proof. So it is imperative that we can restore supply very fast.

Now VECTOR has installed automated switchgear which will ensure that Middlemore is not left with generator-only supply for any length of time in the unlikely event of an outage.

Middlemore can now be supplied by either one of two VECTOR zone substations – Hans to the North, or Mangere Central to the south.

If power goes off due to a fault between the substation and Middlemore, VECTOR operators are immediately alerted by a computer screen at our 24-hour system control in Newmarket – automation then allows them to flick a remote control to switch the feed to the other substation. All other things being equal, this is all completed well within two minutes.

That's a dramatic improvement on waiting for a service vehicle to travel to the area to carry out a manual switchover.

Flicking a remote control may not be as dramatic as a service vehicle racing through a dark, wet night, but this is reality, not ER.

Immediate response times are also important to companies and their manufacturing processes. At Nesdale Avenue in Wiri – home to a string of businesses, including Nestle New Zealand, Kiwi Packaging and Polarland – two feeder lines converge at the top of the street. Now, if one feeder faults between Nesdale Avenue and a substation, smart switching gear automatically selects the feeder that is still transmitting – all within 10 seconds.

Premier service, no drama.

"VECTOR has an underlying ethos of reaching further and knows there is much to be done..."

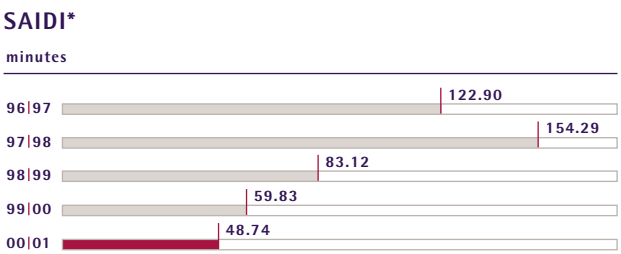
Chief Executive's Review Reaching Further

VECTOR has made further progress in its second year as a pure distribution network company. The strong, ahead-of-target financial outcomes, covered in the Chairman's report, have been achieved with prices continuing to be held flat. Our residential rates remain the lowest of New Zealand's major centres.

To maintain this will demand superior asset management. The company's performance in these areas is starting to reflect the importance we have placed on it, particularly through innovative application of technology and automation.

However, VECTOR is much more than an asset manager – it is a service company which must provide customers with accessibility, accountability, responsiveness and clear information. Concentrated effort has gone into all of these areas and we have lifted our game considerably, as shown in the tangible measures summarised below.

However, VECTOR has an underlying ethos of reaching further and knows there is much to be done before we can claim to have reached our goal of being a premier infrastructure operator.



*(System Average Interruption Duration Index – the industry network reliability measure)

Improving Customer Service

Historically, distribution companies have been asset and engineering-driven, but there is a clear need in the 21st century to see all daily operating issues and future initiatives from a customer perspective.

In this respect, it is pleasing to report that:

- Reliability has again improved, with the system average interruption duration index (SAIDI) brought below 50 minutes – a further improvement on last year's record low 59 minutes.
- For high voltage faults system-wide, we restored 98 per cent of customers' supply within three hours – and over 95 per cent within two hours - reflecting a switch in focus from the engineering approach (repair) to the customer approach (restore, then repair).
- Call-centre performance was excellent, with more than 82 per cent of calls answered within 20 seconds – VECTOR is distinctive in having a direct faults call-centre, and we believe our customers are receiving superior faults response as a result.
- Independent surveys show that customer satisfaction with our field staff has lifted further – VECTOR's service people are now clearly branded in the field, a 1999 initiative to improve accountability.
- A special health and safety programme has seen a dramatic reduction in lost time injury frequency rate (LTIFR) – the year was completed with five successive months with no lost time injuries.
- VECTOR moved quickly and smoothly to lead lines companies in offering a 90 percent variable charge to residential customers.

Finally, we have launched a dedicated Key Account Manager programme for our large customers, reflecting their special requirements as the country's major manufacturers and service companies. This is already lifting performance, particularly in understanding and responding to power quality issues.

Not all our initiatives have started smoothly. The LineCare service introduced in mid-year has been a major success in streamlining fault response. However, we drew a negative response to its initial pricing, which we addressed.

Network Upgrading

Ultimately, the standard of service we can offer will be limited by the quality and condition of the network.

We have continued to focus on using smarts and technology to lift the performance and utilisation of our existing assets. The Onehunga and Kawakawa Bay automated switching solutions are now well-advanced: both use innovative approaches to avoid the need for the multi-million dollar capital programmes which traditional methodology would have dictated. Similarly, state-of-the-art programmes for real-time monitoring of assets, and probabilistic design techniques, are bearing fruit.

But with elements of the network being now over 70 years old, some capital reinvestment is necessary. As the Chairman notes, we are completing a major renewal and reinforcement of our transmission and subtransmission system, which will support the region's needs for years to come.

Our investigations show we also need to perform significant asset renewal in the low voltage system over the next three to five years, if we are to achieve the performance our customers require. This will include targeted replacement of underperforming equipment, which can number in the tens of thousands.

A huge difficulty is that insufficient records were kept historically to either locate them or to analyse their performance: this we are overcoming.

Our first three major low voltage improvement programmes will start early in the new financial year.

The Way Ahead

The network challenges ahead include:

- More investment in customer service areas, including linking the company's geographical information system (GIS) with the computerised customer management system and a new SCADA control and distribution management system.
- Continued refinement of our network and asset modeling and monitoring, to enhance performance and refine risk management.
- More automated switching to boost the company's ability to get the power back on more quickly and, with a focus on demand-side management and conservation, to lift our asset utilisation.
- Implementing differentiated services at differentiated pricing to meet the needs of individual customers.

To achieve this, we will continue to invest heavily in upskilling staff, including both training and participation in international distribution technology forums.

Industry Environment

The restructuring imposed on the electricity industry by the 1998 legislation has led to dislocations and difficulties, and set back customer service. The legislation now being mooted has been more considered, but we must ensure we do not revert to centrally mandated performance and pricing structures – a one size fits all approach.

This would be fundamentally flawed.

Any requirement that seeks to impose a uniform service standard misses the point that distribution businesses must provide levels of reliability, quality and response scaled to fit differing consumer needs at differing prices.

VECTOR is not against guaranteeing service levels – in fact, we lead in doing this - but it understands that one standard does not fit all needs.

We also believe the appropriate point of customer interface for service must be the distribution company and welcome the recognition this is beginning to get across the country. The distribution company has the

physical connection with customers and controls almost all the quality and service issues. And in times where customers frequently switch energy retailers, the electricity distribution company has a more permanent relationship with consumers.

Development

We have been prudent to date, and will remain so, investing only where our competencies or systems allow us to create value. However, it is pleasing to note:

- Our successful launch during the year of Tangent, our next generation telecommunications network owner; and
- The pending incorporation of Stream Information Limited, a joint venture (in which VECTOR holds a 70 per cent interest) providing independent metering, measurement and information services to time-of-use customers nationally.

There are other opportunities opening for VECTOR, as the new industry structure emerges. Customers are seeking enhanced services which we are well-positioned to provide; also many of New Zealand's lines companies do not have the scale or the systems to provide the service which will be demanded of them, and this is an opportunity.

The VECTOR Team

Our key to continued development is our people. I would like to record my congratulations to the wider VECTOR team – our staff and those of our contractors – on their achievements in the year under review.

We have significant challenges ahead, but I am confident they have the drive and competency to understand and meet the needs of the cosmopolitan customer base we serve.

Patrick Strange, Chief Executive

Upgrade Passes With Flying Colours

Switching over to the upgraded Inner Auckland power system has required all the preparation, precision and assuredness of a chess master at play against the time clock.

There was no "big bang" transformation from the old to the new. Switchover and testing of the cabling, substation equipment and state-of-the-art protection and control systems has been a long and exacting task. The step-by-step moves have had to be carried out with great care. Like chess, each step was irreversible and had to be accomplished correctly the first time round: there was no second chance.

And now that the new system has passed its tests, the line that has kept the central city in business since 1998, the temporary overhead link, is being taken away. In its place is a network that is very much stronger and more durable than ever before.

The multi-year project to replace the old with the new has cost nearly $200 million and the end result is an enhanced electricity infrastructure that can support the new century's growth. It will not only cope with rising demand but provide more flexibility for both Inner Auckland and other suburbs, through enhanced interconnections, while upgrading northern North Island transmission security.

While the best-known feature of the new system is the 3-metre diameter, 9.2-kilometre long tunnel running under the Southern Motorway and city streets from Transpower's national grid substation at Penrose to the CBD, the upgrade project comprised a number of vital components, including:

- The tunnel-carried supply, comprising two 110,000 volt circuits, each circuit consisting of three 110mm diameter cables
- A new 110,000 volt cable trench-laid from the national grid substation at Mt Roskill to the CBD
- New 22,000 volt links around the inner city area
- A new 33,000 volt link laid in the tunnel to reinforce supply to Newmarket
- New high-voltage substations at Hobson Street and Liverpool Street
- Other extensive substation upgrading, including modern, new transformers and latest technology switchgear.

The whole programme has been VECTOR's largest-ever capital works scheme.

The tunnel alone was huge. Construction began in May 1997, with a roadheader working south from the CBD waterfront and a specialist tunnel boring machine – twice the length of a rugby field – driving north from Penrose. Holethrough – when the two met, within millimetres of exact alignment - occurred 100 metres below Khyber Pass in January 2000.

After breakthrough, the earth and rock walls of the tunnel were lined with concrete and grouted, and tunnel ventilation, fire protection and communications equipment were installed. In addition, tracks were laid for the custom-built, rail-mounted vehicle that will carry maintenance teams along the tunnel.

The laying of the cables themselves on stainless steel racks was a demanding task. Each cable has an aluminium conductor surrounded by cross-linked polyethylene insulation and an outer sheath of corrugated stainless steel, coated with a layer of high-density polyethylene for mechanical and corrosion protection. Not surprisingly, each 1300-metre drum of cable weighed a hefty 25 tonnes – not forgetting that there are two circuits, each comprising three cables.

Further protecting this major artery is a safety and security system that includes huge concrete lids weighing 25 tonnes at each access shaft, and special security doors.

The demanding testing and switching phase for the total reinforcement project took the best part of three months – a small wait given the new life the upgrade programme has brought to Auckland's infrastructure. And it was achieved without so much as a minute of customer interruption.

Big Benefits from Safety Focus

Our front-line VECTOR teams have a dangerous job. High voltage, trenches, working at night, at height, underground, in traffic and in all weather.

With these working conditions, it's essential that VECTOR places a huge emphasis on safety.

Not only for our staff, contractors and sub-contractors, but also for the community. By protecting ourselves and our equipment, we're also making the environment in which our customers work and live safer. But our focus goes beyond keeping people from harm. Safety is all about systems, training and worksite planning. Ultimately, these are the same disciplines that deliver quality, reliability and productivity, and the benefits flow-on to better pricing and service levels for our customers.

Over the past two years, VECTOR has made a major push toward transforming our safety record. It's been a gratifying success thus far, with the company now ranking with the best of the Australian network companies. And our performance has lifted with it.

As recently as 1996, our employees and contractors suffered 80 lost time injuries, at a rate of 6.6 per month. This means that for every one million hours worked, 80 accidents were severe enough to stop the worker from resuming duties within 24 hours. This compares to the final five months of 2001, when not one lost time injury was reported – proof of our markedly improved safety performance.

But we're not satisfied. We want to lift our performance to that attained by top manufacturing companies in the world.

Part of our strategy is about making our assets safer, with several multi-million dollar replacement programmes completed or planned. But more, it's about our people, their training and attitude.

We take a zero-tolerance attitude to accidents and Aucklanders can help. Next time you see one of our VECTOR crew working urgently on a wet city street to restore power to customers, they'll be wearing high visibility safety gear and being as careful as they can, but they're still vulnerable. So please slow down and watch out for them.

And while our customers aren't working with high-voltage equipment, there's still plenty to learn from our experience. On our website (www.vector-network.co.nz), we've got safety tips for work and home.