

Interim Report

2002



FOR THE SIX MONTHS ENDED 30 SEPTEMBER 2002



Chairman's Report

The directors of VECTOR are pleased to advise an unaudited after-tax net surplus of \$42 million for the six months to 30 September 2002, compared with \$44 million in the same period the previous year. Operating surplus (earnings before interest, tax, depreciation and amortisation) for the 2002 half-year was \$78.5 million, as against \$88.8 million in the comparative period.

While both figures were below those for 2001, due to a significant reduction in pricing and a planned increase in the amount of network maintenance carried out, they were ahead of budget in each case. VECTOR reduced its prices from April 2002 by 10 per cent, on average, for residential customers, and by as much as 25 per cent for the 30,000 small commercial customers.

Total revenue, at \$133.5 million, was also down, as expected, on the previous year's \$137.1 million, but ahead of budget as a result of higher power usage due to cooler weather.

A rise in total assets from \$1,037.1 million to \$1,097.5 million in the comparative periods reflected investments in UnitedNetworks shares prior to the completion of the acquisition, partly offset by lower levels of cash on deposit.

The half-year results were achieved prior to the company's acquisition of UnitedNetworks.

Overall, VECTOR has achieved a strong result and it is gratifying to record further improvements across almost all aspects of the company's core business.

In the first six months of this financial year, the company continued to invest in automation and technology, producing further operational efficiencies and customer benefits.

It is most rewarding to see these efforts have been recognised on the international stage. In August, VECTOR won the prestigious GITA excellence award for the best application of computerised Geographic Information System (GIS) technology in the Australasian region.

Investment has not just been restricted to technology. One of the most important investments this year has been in VECTOR's major undergrounding programme,

with several large projects already under way. A key achievement has been to pioneer a "dig once" approach, which involves VECTOR partnering with other utilities and councils to coordinate all undergrounding work at one time to revitalise neighbourhoods.

The company has made significant improvements across all aspects of the business but more importantly, is committed, now more than ever, to continually raising the bar.

Changes in the regulatory environment lie ahead. The company has taken an active and constructive role in providing input on the proposed changes, as the directors consider it vital that VECTOR's ability to innovate and continue to create value for customer and shareholder alike be maintained. Also, the integration of the VECTOR and UnitedNetwork businesses to create New Zealand's largest electricity and gas network, which is proceeding to plan, must be completed. These are challenges that I am sure the board, management and staff will rise to with equal resolve and success.

The board would like to acknowledge the outstanding contribution made by Dr Patrick Strange, VECTOR's chief executive since the company was formed in April 1999. It was announced on 20 December 2002 that he would retire, and would be replaced from 1 February 2003 by Mark Franklin, who has had extensive experience in the energy and technology sectors in New Zealand, Australia and Japan. In Patrick Strange's time the company has become an industry leader and gone from strength to strength, culminating in the \$1.5 billion UnitedNetworks acquisition. He leaves VECTOR in a very sound position, and the board wishes him well in the future.



MICHAEL STIASSNY
Chairman

for the six months ended 30 September 2002

Consolidated statement of financial performance

| | | UNAUDITED SIX MONTHS ENDED 30 SEPTEMBER | | AUDITED YEAR ENDED 31 MARCH |
|--|-------|---|----------|-----------------------------------|
| Notes | 2002 | 2001 | 2002 | |
| | \$000 | \$000 | \$000 | |
| Operating revenue | 2 | 133,539 | 137,078 | 241,251 |
| Operating expenses | 3 | (76,568) | (69,444) | (144,929) |
| Operating surplus before income tax | | 56,971 | 67,634 | 96,322 |
| Income tax expense | | (14,962) | (23,764) | (34,959) |
| Operating surplus after income tax | | 42,009 | 43,870 | 61,363 |
| Minority interest in deficit of partnership | | 26 | 130 | 320 |
| Net surplus | | 42,035 | 44,000 | 61,683 |
| Comprising | | | | |
| Net surplus from continuing activities | | 42,047 | 43,946 | 61,948 |
| Net surplus / (deficit) from discontinued activities | | (12) | 54 | (265) |
| | | 42,035 | 44,000 | 61,683 |

Consolidated statement of movements in equity

| | Notes | UNAUDITED SIX MONTHS ENDED 30 SEPTEMBER | | AUDITED YEAR ENDED 31 MARCH |
|--|-------|---|-----------------|-----------------------------------|
| | | 2002 \$000 | 2001 \$000 | 2002 \$000 |
| Equity at beginning of period | | 716,697 | 730,427 | 730,427 |
| Net surplus | | 42,035 | 44,000 | 61,683 |
| Movement in revaluation reserve | 4 | - | (73,061) | (76,422) |
| Total recognised revenues and expenses for the period | | 42,035 | (29,061) | (14,739) |
| Minority interest in partnership | | (26) | 1,199 | 1,009 |
| Distributions to owners | | (42,800) | - | - |
| Equity at end of period | | 715,906 | 702,565 | 716,697 |

as at 30 September 2002

Consolidated statement of financial position

| | UNAUDITED SIX MONTHS ENDED 30 SEPTEMBER | | AUDITED YEAR ENDED 31 MARCH |
|---|---|------------------|-----------------------------------|
| Notes | 2002 | 2001 | 2002 |
| | \$000 | \$000 | \$000 |
| Equity | | | |
| Share capital | 300,000 | 300,000 | 300,000 |
| Reserves | 4 358,113 | 361,474 | 358,113 |
| Retained earnings | 56,810 | 39,892 | 57,575 |
| Shareholders' equity | 714,923 | 701,366 | 715,688 |
| Minority interest | 983 | 1,199 | 1,009 |
| Total equity | 715,906 | 702,565 | 716,697 |
| Non-current liabilities | | | |
| Borrowings (secured) | 948 | 104,810 | 338 |
| Deferred tax | 101,300 | 74,070 | 90,232 |
| Total non-current liabilities | 102,248 | 178,880 | 90,570 |
| Current liabilities | | | |
| Accounts payable and accruals | 69,393 | 45,047 | 48,452 |
| Income tax | 4,261 | 26,540 | 4,300 |
| Current portion of borrowings (secured) | 205,703 | 84,076 | 150,763 |
| Total current liabilities | 279,357 | 155,663 | 203,515 |
| Total liabilities | 381,605 | 334,543 | 294,085 |
| Total equity and liabilities | 1,097,511 | 1,037,108 | 1,010,782 |
| Non-current assets | | | |
| Non-current receivables | 1,500 | - | 1,000 |
| Goodwill | 3,545 | 3,765 | 3,568 |
| Investments | 73,634 | - | - |
| Property, plant and equipment | 964,237 | 960,626 | 961,410 |
| Total non-current assets | 1,042,916 | 964,391 | 965,978 |
| Current assets | | | |
| Cash | 6,127 | 20,452 | 6,128 |
| Receivables and prepayments | 48,468 | 52,265 | 38,676 |
| Total current assets | 54,595 | 72,717 | 44,804 |
| Total assets | 1,097,511 | 1,037,108 | 1,010,782 |

Consolidated statement of cash flows

| | UNAUDITED SIX MONTHS ENDED 30 SEPTEMBER | | AUDITED YEAR ENDED 31 MARCH |
|---|---|---------------|-----------------------------------|
| | 2002 | 2001 | 2002 |
| | \$000 | \$000 | \$000 |
| Cash flows from operating activities | | | |
| Cash inflows | 124,759 | 124,183 | 238,922 |
| Cash outflows | (76,061) | (63,031) | (133,554) |
| Net cash inflow from operating activities | 48,698 | 61,152 | 105,368 |
| Cash flows from investing activities | | | |
| Cash inflows | 1,686 | 3,901 | 6,267 |
| Cash outflows | (63,135) | (24,976) | (48,097) |
| Net cash outflow from investing activities | (61,449) | (21,075) | (41,830) |
| Cash flows from financing activities | | | |
| Cash inflows | 55,550 | 24,076 | - |
| Cash outflows | (42,800) | (48,000) | (61,709) |
| Net cash inflow / (outflow) from financing activities | 12,750 | (23,924) | (61,709) |
| Net increase / (decrease) in cash held | (1) | 16,153 | 1,829 |
| Cash balance at beginning of period | 6,128 | 4,299 | 4,299 |
| Cash balance at end of period | 6,127 | 20,452 | 6,128 |

for the six months ended 30 September 2002

Consolidated operating cash flow reconciliation

| | UNAUDITED SIX MONTHS ENDED 30 SEPTEMBER | | AUDITED YEAR ENDED 31 MARCH |
|--|---|---------------|-----------------------------------|
| | 2002 | 2001 | 2002 |
| | \$000 | \$000 | \$000 |
| Reported net surplus after tax | 42,035 | 44,000 | 61,683 |
| Minority interest in deficit of partnership | (26) | (130) | (320) |
| | 42,009 | 43,870 | 61,363 |
| Add / (less) non-cash items | | | |
| Depreciation and amortisation | 16,711 | 15,616 | 31,677 |
| Movement in deferred tax | 11,068 | 1,783 | 17,945 |
| Gain on sale of fixed assets | (566) | (2,572) | (1,904) |
| Other non-cash items | (722) | (633) | (1,026) |
| | 26,491 | 14,194 | 46,692 |
| Add / (less) movement in working capital | | | |
| Accounts payable and accruals | (9,006) | (3,520) | 1,368 |
| Receivables and prepayments | (10,757) | (9,304) | 2,273 |
| Provision for income tax | (39) | 15,912 | (6,328) |
| | (19,802) | 3,088 | (2,687) |
| Net cash inflow from operating activities | 48,698 | 61,152 | 105,368 |

1. ACCOUNTING POLICIES

The interim financial statements have been prepared having regard to the requirements of the New Zealand Stock Exchange and those of Financial Reporting Standard No. 24 – Interim Financial Statements. As the disclosure required in the interim financial statements is less extensive than in the annual financial statements, the interim financial statements should be read in conjunction with the previous annual financial statements for the year ended 31 March 2002.

The accounting policies used in preparation of the interim financial statements are consistent with those used in preparing the annual financial statements for the year ended 31 March 2002.

For the year ended 31 March 2002, the Group changed its accounting policy in respect of accounting for dividends. Under the new policy, dividends are only brought to account in the period in which they are declared. The Board of Directors adopted this change in accounting policy to conform with the requirements of Financial Reporting Standard No. 5 – Events Occurring After Balance Date. Thus, the dividend of \$42.8 million paid on 31 July 2002 has been brought to account in the six months ended 30 September 2002. The dividend of \$48.0 million paid in the corresponding period to 30 September 2001 had previously been recorded as a distribution in the financial statements for the year ended 31 March 2001.

In addition, in the year ended 31 March 2002, the Group changed its accounting policy in respect of accounting for income tax. Under the new policy, all timing differences in respect to property, plant and equipment are recognised, including those arising from revaluations. Previously, timing differences in relation to revaluations of property, plant and equipment not expected to crystallise in the foreseeable future were not recognised. The change in policy resulted in an increase of \$65.0 million to the deferred tax liability and a decrease of the same amount to the asset revaluation reserve. Because the revaluation has previously been recognised directly in the revaluation reserve, the tax effect has also followed this treatment and been taken directly to the revaluation reserve. This policy has been applied consistently for the periods ended 30 September 2001, 31 March 2002 and 30 September 2002.

2. OPERATING REVENUE**Trading revenue**

| | UNAUDITED SIX MONTHS ENDED 30 SEPTEMBER | | AUDITED YEAR ENDED 31 MARCH |
|------------------------------|---|----------------|-----------------------------------|
| | 2002 | 2001 | 2002 |
| | \$000 | \$000 | \$000 |
| Trading revenue | | | |
| Sales | 127,488 | 130,581 | 230,511 |
| Investment revenue | | | |
| Interest revenue | 584 | 374 | 683 |
| Other revenue | | | |
| Miscellaneous income | 4,834 | 3,486 | 8,153 |
| Gain on sale of fixed assets | 633 | 2,637 | 1,904 |
| | 133,539 | 137,078 | 241,251 |

Investment revenue**Other revenue****3. OPERATING EXPENSES****Include:**

4. REVALUATION RESERVE

During the year ended 31 March 2002 the group recognised a deferred tax liability of \$65.0 million in relation to its change in accounting policy on accounting for income tax, which reduced the revaluation reserve accordingly.

In addition, an adjustment was made to the depreciated replacement cost (DRC) valuation of distribution assets which resulted in a reduction of the revaluation reserve.

5. COMMITMENTS

Capital expenditure commitments

Estimated capital expenditure contracted but not provided for

9,561

9,405

10,775

Operating lease commitments

Within one year

1,159

1,383

1,172

One to two years

1,140

1,296

1,172

Two to five years

1,768

3,609

2,302

Beyond five years

87

186

113

4,154

6,474

4,759

6. CONTINGENT LIABILITIES

As at 30 September 2002 VECTOR Limited had made a conditional offer for 100% of UnitedNetworks Limited, which was subsequently accepted as explained in Note 8.

7. INVESTMENTS

During September 2002 VECTOR Limited acquired on market a 5.0% share in UnitedNetworks Limited.

8. EVENTS OCCURRING AFTER BALANCE DATE

On 11 October 2002, VECTOR Limited acquired a further 70.2% of the shares in UnitedNetworks Limited. VECTOR Limited purchased the remaining shares in UnitedNetworks Limited by 15 November 2002.

During October and November 2002 VECTOR Limited issued Capital Bonds with a principal value of \$307,205,000. The bonds have an initial term of four years and currently attract interest of 8.25% per annum.

As the above transactions occurred after balance date the financial effect has not been recognised in the financial statements.

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