

Eraring Energy

AUDIT OPINION

The audit of Eraring Energy and its controlled entity's financial report for the year ended 30 June 2008 resulted in an unqualified Independent Auditor's Report.

The auditor's report included an emphasis of matter paragraph drawing attention to Eraring Energy's power station and equipment valuation. The valuation is determined by using estimated discounted cash flows. These cash flows are subject to significant uncertainty arising from the Federal Government's proposed Carbon Pollution Reduction Scheme.

PERFORMANCE INFORMATION

Operational Performance

Eraring Energy operates a diverse portfolio of generating assets comprising thermal coal, hydro and wind. Most of its generation comes from Eraring Power Station, which uses thermal coal. Eraring Power Station produced 17,283 gigawatt hours of electricity in 2008. This is similar to the previous year's record level.

Some of the indicators Eraring Energy uses to assess its electricity generation performance are shown below.

Year ended 30 June	Actual					Target*
	2004	2005	2006	2007	2008	2008
Generation of electricity (gigawatt hours)						
Thermal coal	14,567	12,703	14,216	17,530	17,283	17,500
Hydro	171	202	309	114	92	259
Wind	27	28	26	24	24	28
Total	14,765	12,933	14,551	17,668	17,399	17,787
Plant availability (%)	89.6	85.9	86.9	93.0	92.5	93.2
Thermal efficiency (%)	38.2	37.9	37.9	37.9	37.9	37.9

Source: Eraring Energy.

* Target agreed with shareholder Ministers in the Statement of Corporate Intent.

Renewable energy sources of hydro and wind accounted for 0.67 per cent of total production (0.78 per cent in 2006-07). The trend for lower hydro production is due to the continuing effect of drought.

Plant availability measures the total time Eraring Power Station's generating units were either in service or able to be placed in service over a given period.

Thermal efficiency indicates the percentage of energy contained in the coal used by Eraring Power Station to produce the electricity. The quality of energy fuel used and plant performance determine thermal efficiency.

Consolidated Financial Performance

	Actual					Target*
	2004	2005	2006	2007	2008	2008
Earnings before interest and tax from normal operations (\$m)(a)	157.2	181.4	182.4	272.4	270.2	171.7
Return on equity (%) (b)	6.1	6.9	11.0	34.6	8.3	5.3
Return on assets (%) (c)	7.3	8.0	7.1	6.9	7.3	4.7
Interest cover (times)	8.9	10.0	7.2	13.8	9.1	3.7
Total distributions to government (\$m) (d)	98.1	115.7	97.0	193.8	159.1	76.1
Capital expenditure (\$m)	33.0	43.4	36.3	38.0	55.0	61.3

* Target agreed with shareholder Ministers in the Statement of Corporate Intent and excludes fair value movements in superannuation, financial instruments and insurance provision.

(a) Excludes fair value movements in electricity derivatives, superannuation and insurance provision movements.

(b) Net profit after tax (excluding fair value movements in electricity derivatives, superannuation and provision movements) divided by total equity.

(c) Earnings before interest and tax from normal operations divided by total assets.

(d) Total distribution before adjustment for Community Service Obligation.

Financial ratios achieved during the year generally exceeded agreed targets.

OTHER INFORMATION

Major Project Expenditure

The Black Start Gas Turbine at the Eraring Power Station was commissioned and installed by March 2008. This project provides quick re-start in the event of a system wide black out. Total project expenditure of \$25.3 million compares favourably with budgeted costs.

A capacity upgrade and performance improvements at the Eraring Power Station were approved in June 2008. The nominal capacity of each of the Station's four units will increase from 660 megawatt to 720 megawatt. The works include construction of a cooling water attemperation reservoir used to manage cooling water exit temperatures. The reservoir is due for completion by August 2009.

Coal Supply

Coal prices have increased significantly in recent years. With Eraring Energy's reliance on coal, this presents challenges for the organisation to manage costs. Contracts are in place for a significant proportion of future years' coal requirements. Eraring Energy is exploring strategies to minimise risks associated with increasing coal costs.

Contractor's Claim

Eraring Energy settled a claim for extra costs from a contractor involved in the 2002 upgrade of Burrinjuck Hydro Power Station. Settlement of legal costs is still in dispute, but resolution is expected in 2008-09.

Electricity Reform - development sites

The Government's electricity reform package proposes selling development sites to private operators. Eraring Energy holds no such sites and would not be impacted by these proposals.

FINANCIAL INFORMATION

The following consolidated financial information is for Eraring Energy and its controlled entity, Pacific Western Pty Limited.

Abridged Income Statement

Year ended 30 June	2008 \$'000	2007 \$'000
REVENUE		
Electricity sales and other	726,163	876,847
Electricity Tariff Equalisation Fund	16,111	(32,617)
PROFIT BEFORE BORROWING COSTS, DEPRECIATION AND TAX	260,278	292,514
Borrowing costs	19,528	14,663
Depreciation	92,794	69,979
PROFIT BEFORE TAX	147,956	207,872
Income tax equivalent expense	44,729	62,197
PROFIT AFTER TAX	103,227	145,675
Dividend provided	114,594	132,131

Revenue included \$714 million in electricity sales compared to \$849 million in the previous year. The decrease was due to lower spot prices primarily brought about by the easing of the drought risk in the electricity market. Lower electricity sales revenue was supplemented by receipts from the Electricity Tariff Equalisation Fund (ETEF) of \$16.1 million. High sales figures in 2007 meant Eraring Energy made payments of \$32.6 million to the ETEF.

Abridged Balance Sheet

At 30 June	2008 \$'000	2007 \$'000
Current assets	136,371	552,610
Non-current assets	2,303,157	2,368,997
TOTAL ASSETS	2,439,528	2,921,607
Current liabilities	320,285	1,638,557
Non-current liabilities	780,134	903,046
TOTAL LIABILITIES	1,100,419	2,541,603
NET ASSETS	1,339,109	380,004

Eraring Energy's balance sheet has significantly changed from the prior year. Most of the changes arise from the impact of derivatives. Changes in forward electricity prices and a reduction in derivative activity at year-end resulted in reductions in current and non-current liabilities. Current and non-current asset reductions are also largely attributable to derivative impacts. Further detail on the impact of derivatives on balance sheets appears in the 'Electricity Industry Overview' earlier in this report.

Offsetting the reduction in non-current assets from derivatives is an increase in property, plant and equipment of \$281 million. Electricity generation assets are valued based on estimated discounted cash flows. Most of the \$281 million is attributable to expected increases in future cash flows arising from higher forward electricity prices.

In 2008, Eraring repaid capital of \$73.4 million to The Treasury (\$184 million in 2006-07) funded by increased borrowings with New South Wales Treasury Corporation. The Board provided for a dividend of \$115 million to be paid to The Treasury (\$132 million).

The overall impact of the transactions and events discussed above is a significant increase in net assets.

MINISTERIAL DIRECTIONS

No ministerial directions were issued by the portfolio Minister during 2007-08 under section 20P of the *State Owned Corporations Act 1989* (the 'SOC Act').

On 21 July 2008, Eraring received a direction to form a new subsidiary that was to enter into agreements to acquire Integral Energy's retail business effective 1 August 2008. This occurred as a consequence of the Government's then energy restructure strategy. On 1 September, after the Government had announced it would not proceed with this particular strategy, Eraring received a policy instruction from The Treasury to terminate the acquisition arrangements, such that Eraring would be in the same position had the acquisition not occurred.

CORPORATION ACTIVITIES

See the 'Electricity Industry Overview' section earlier in this report for general industry comment.

Eraring Energy was established as a statutory State owned corporation in July 2000 under the *State Owned Corporations Act 1989*, *Energy Services Corporations Act 1995* and Energy Services Corporation (Eraring Energy) Regulation 2000. It commenced operations in August 2000 to generate electricity for sale in the National Electricity Market.

For further information on Eraring Energy, refer to www.eraring-energy.com.au.

CONTROLLED ENTITY

Pacific Western Pty Limited has not been reported on separately as it is not considered material by its size or the nature of its operations to the consolidated entity. The entity was de-registered on 28 July 2008 following voluntary liquidation.