
Macquarie Generation

AUDIT OPINION

The audit of Macquarie Generation's financial report for the year ended 30 June 2008 resulted in an unqualified Independent Auditor's Report.

The Independent Auditor's Report included a 'significant uncertainty' paragraph regarding the effect of the Carbon Pollution Reduction Scheme.

Impact of the Carbon Pollution Reduction Scheme

The Federal Government has proposed a Carbon Pollution Reduction Scheme (Scheme), but has not settled how it will operate. Until this occurs, the effect of the Scheme on Macquarie Generation's assets cannot be determined and Macquarie Generation has not taken this into account when applying the requirements of Accounting Standard AASB 136 'Impairment of Assets'.

KEY ISSUES

Development Sites

Macquarie Generation may be required to sell its development sites to private operators, as part of the revised Government's electricity reform package, introduced to secure the future supply of electricity in New South Wales.

Macquarie Generation has two development sites, Tomago Gas Fired Power Station and Coal Baseload - 'Bayswater 2 (B2)'.

Tomago Gas-Fired Power Station

Development approval was granted in December 2003 for the construction of a gas-fired power station at Tomago. The project qualifies as a project of State significance for the New South Wales Government, and therefore requires approval by the Budget Committee to commence. To date, no approval has been granted. The development approval expires in November 2008 in the absence of any commencement of works. Macquarie Generation has received advice that the commencement of geo-technical testing and preparation of the site should allow the continuation of the development approval past November 2008.

Coal Baseload - 'Bayswater 2 (B2)'

Macquarie Generation has completed a feasibility study on a new coal-fired generating plant in the Hunter Valley, known as B2.

The B2 project proposes to build up to two 1,000 megawatt coal-fired generators.

B2 will be designed to run at much higher capacity factors than existing facilities producing outputs of around 15,000 gigawatt hours (GWh) or 20 per cent of New South Wales' energy requirements.

Coal Supply

Coal prices have increased significantly in recent years with the continued demand for Australia's coal for export. This has resulted in increased risks for securing adequate supplies of coal and managing the cost of these supplies.

Macquarie Generation has locked in a significant proportion of its coal supply contracts for the next ten years and it is examining options to manage future supply.

Macquarie Generation's new large rail unloading facility at Antiene was commissioned in July 2007 and will progressively take over the increasing rail coal deliveries from the existing smaller Ravensworth facility. Antiene is designed to service both the Wilpinjong and Anvil Hill coal mines and any future mines to the north and west of Macquarie Generation's power stations.

PERFORMANCE INFORMATION

Operational Performance

Year ended 30 June	2005	2006	2007	2008
Generation of electricity (gigawatt hours sent out)				
Bayswater	16,867	16,540	14,310	15,430
Liddell	9,737	10,057	10,825	10,851
Total	26,604	26,597	25,135	26,281
Plant availability				
Bayswater (%)	87.0	90.1	89.8	91.5
Liddell (%)	81.9	76.9	85.5	78.9
Thermal efficiency				
Bayswater (%)	36.0	35.8	34.9	35.4
Liddell (%)	32.5	32.6	33.2	33.2
Equivalent forced outages (%)	2.3	5.1	4.9	5.4

Macquarie Generation has a policy of not disclosing operational performance targets. Accordingly, these have not been included in the above table.

Macquarie Generation's market share of the National Electricity Market was 13 per cent in June 2008 (12.3 per cent in June 2007). Its market share increased slightly due to water resources increasing compared to the previous year, resulting in higher production.

Financial Performance

Year ended 30 June	Actual		Target*
	2007	2008	2008
Earnings before interest and tax (\$m)	342.6	660.1	253.3
Return on equity (%)	--**	34.2	18.9
Return on assets (%)	8.8	14.8	8.5
Interest cover (times)	5.8	15.0	4.2
Debt to equity (%)	--**	45.6	85.4
Total distributions to government (\$m)	264.8	454.4	188.0
Capital expenditure (\$m)	166.4	83.0	130.4

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

** Ratios are not meaningful as a result of negative equity.

Financial ratios exceeded targets and prior year actuals due to earnings before interest and tax exceeding target by \$407 million (161 per cent) and previous year actuals by \$317 million (93 per cent). The main contributor was an increase in unrealised income associated with movements in the fair value of electricity derivatives from unrealised losses in 2006-07 of \$95.9 million to unrealised gains of \$249 million in 2007-08.

Capital expenditure decreased by \$83.4 million over the prior year primarily due to the completion of the construction of the Antiene rail coal unloader.

Capital expenditure included \$19.8 million for the ongoing construction of the water treatment plant (Bayswater) and \$19.6 million for the \$50.0 million upgrade of the current Hunter River pumping station.

Distributions to government increased by \$190 million (72 per cent) from the previous year due to dividends increasing by \$90.0 million and income tax expense increasing by \$100 million as a result of the higher earnings before interest and tax.

OTHER INFORMATION

We identified some opportunities for improvement in internal controls and procedures. These have been reported to management.

FINANCIAL INFORMATION

Abridged Income Statement

Year ended 30 June	2008 \$'000	2007 \$'000
TOTAL REVENUE	1,162,402	1,082,037
PROFIT BEFORE BORROWING COSTS, DEPRECIATION AND TAX	790,118	457,561
Finance costs	<i>62,557</i>	66,985
Depreciation	<i>111,663</i>	106,852
PROFIT BEFORE TAX	615,898	283,724
Income tax equivalent expense	<i>184,431</i>	84,808
PROFIT AFTER TAX	431,467	198,916
Dividend provided	<i>270,000</i>	180,000

Profit after tax of \$431 million was up \$233 million on the previous year, including unrealised gains on derivative contracts of \$251 million reflecting the positive effect of the falling forward electricity prices.

Abridged Balance Sheet

At 30 June	2008 \$'000	2007 \$'000
Current assets	750,965	784,910
Non-current assets	3,699,109	3,091,361
TOTAL ASSETS	4,450,074	3,876,271
Current liabilities	856,465	2,051,514
Non-current liabilities	1,793,764	1,882,170
TOTAL LIABILITIES	2,650,299	3,933,684
NET ASSETS/(LIABILITIES)	1,799,845	(57,413)

Non-current assets increased by \$608 million, largely due to a \$1.1 billion revaluation of Property, Plant and Equipment in 2007-08, offset by a reduction in deferred tax assets of \$435 million.

The lower spot prices and a decreasing electricity forward price curve significantly reduced current liabilities compared to the prior year.

CORPORATION ACTIVITIES

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

Macquarie Generation operates the Bayswater and Liddell coal-fired power stations in the Upper Hunter Valley.

Macquarie Generation was constituted in March 1996 as an electricity generator under the *Energy Services Corporations Act 1995* and as a statutory State owned corporation under the *State Owned Corporations Act 1989*. The voting shareholders are the Treasurer and the Minister for Finance.

For further information on Macquarie Generation, refer to www.macgen.com.au.