



21 December 2017

## **Contact Energy to sell AGS to Gas Services New Zealand (GSNZ)**

Contact Energy Limited (Contact) has announced the sale of its Ahuroa Gas Storage facility (AGS) to Gas Services New Zealand (GSNZ) for NZ\$200 million, while retaining the rights to use the facility to meet its future needs.

Situated in Taranaki, the AGS facility was opened by Contact in 2010 to store gas for use at its nearby Stratford Power Station. GSNZ is a provider of operational services to First Gas and other customers. GSNZ operates one of New Zealand's largest gas networks, with 2,500 kilometres of high pressure gas transmission pipelines and around 4,800 kilometres of gas distribution pipelines in the North Island.

New Zealand's share of renewable electricity generation is among the highest in the world, and growing, however the high level of hydro-electric generation means the system needs flexible fuel to cope with dry periods and peak demand during winter.

"Gas-fired thermal plant plays a key role supporting renewable generation in New Zealand when hydro generation is below average or during peak demand, and AGS helps us to store gas for use at those times," said Dennis Barnes, CEO Contact Energy.

"By selling AGS to GSNZ we maintain access to a flexible and cost effective fuel supply. The deal has the additional advantage of seeing AGS operated by a dedicated gas infrastructure company, letting us focus on the generation and customer sides of our business."

"I believe with GSNZ as the owner, AGS is more likely to get new customers and we've committed to an initial expansion of AGS to facilitate this. We will receive a reduction on our payments to GSNZ as more customers use AGS," said Barnes.

GSNZ's, Paul Goodeve sees AGS as an important part of New Zealand's gas infrastructure. "Flexibility is one of the major attractions of using natural gas. By expanding the services offered at AGS, we see an opportunity to provide gas producers, shippers and end-users with more flexibility to manage their energy needs."

The proceeds of the sale will be put towards repaying debt and the tax paid on the sale could allow Contact to fully impute the FY2018 target dividend of 32 cents per share.

Until there are additional long term customers of the facility, S&P will capitalise the storage services payments. The S&P net debt / EBITDAF ratio remains substantially unchanged post transaction. Contact expects the transaction to have no impact on its BBB credit rating from S&P.

Completion of the sale of the AGS is subject to the fulfilment of certain conditions set out in the transaction agreements, including receipt of certain regulatory approvals as described in the investor briefing materials.



## **Webcast and audio conference**

Contact Energy's Chief Executive, Dennis Barnes, and Chief Financial Officer, Graham Cockroft, will make a presentation for investors outlining the transaction at 11.00am NZT, Thursday 21 December 2017. An archived replay will be available following the briefing on our website.

If you would like to join the Conference Call.

- You will need to register in advance of the conference using the link provided below. Upon registering, you will be provided with participant dial-in numbers, Direct Event passcode and unique registrant ID.
- In the 10 minutes prior to call start time, you will need to use the conference access information provided in the email received at the point of registering.
- Note: Due to regional restrictions some participants may receive operator assistance when joining this conference call and will not be automatically connected.

### **Direct Event online registration:**

Conference ID **7178357**

<http://apac.directeventreg.com/registration/event/7178357>

For further information please contact:

Investor enquiries:

**Matthew Forbes**

Investor Relations Manager

+64 21 072 8578

Media enquiries:

**Jason Krupp**

Communications Advisor

+64 21 701 898

# INVESTOR BRIEFING

Thursday, 21 December 2017

## Sale of the Ahuroa Gas Storage facility

### Delivering on our strategy through portfolio optimisation

Contact has entered into an agreement to sell the Ahuroa Gas Storage facility and associated assets (AGS) to Gas Services New Zealand (GSNZ), an associate of First Gas Limited, for a cash consideration of NZ\$200 million. As part of the transaction, Contact has retained access to competitive long term gas storage services compatible with its requirements for flexible thermal generation.

Contact's strategy is to optimise the Customer and Generation businesses to deliver strong cash flows which are ultimately for distribution to shareholders. The strategy is underpinned by a disciplined and transparent approach to operating and capital expenditure while ensuring our portfolio of assets are delivering returns for shareholders.

In line with this strategy, Contact identified higher value owners for this long life infrastructure asset and initiated a negotiated sales process to unlock value for shareholders.

### Creating value for Contact shareholders through the commercialisation of AGS

The AGS reservoir is larger than Contact's requirements and is capable of supporting the provision of storage services to other potential customers. GSNZ, as an independent owner of AGS and key gas industry participant, is well placed to accelerate the commercialisation of AGS. With a lower cost of capital and opportunity for a sharing of operational synergies, GSNZ will be a higher value owner of the facility.

To support potential new customers of AGS, GSNZ has committed through to an expansion of the AGS facility within approximately two years of completion of the sale transaction, which will reduce the cost per unit of gas storage services.

Contact preserves long term value by maintaining its capacity rights to the expansion of the AGS facility along with reductions in its annual fee for gas storage services provided by GSNZ where third party customers are contracted by GSNZ.

## **Consideration**

The total consideration for the disposal is NZ\$200 million payable in cash at completion. The sales proceeds arising from the disposal will be subject to income tax payable of approximately \$48 million with net transaction proceeds of NZ\$151 million (after transaction costs of \$1 million) applied to the reduction of debt. The tax payment will result in the creation of additional imputation credits which could allow for the FY18 target dividend of 32 cents per share to be fully imputed.

As a result of the disposal, Contact is expected to record an unaudited estimated gain on the disposal of assets of approximately NZ\$15 million based on the consideration, the carrying value of the assets at 30 November 2017 and the estimated transaction costs.

Until there are additional long term customers of the facility, S&P will capitalise the storage services payments. The S&P net debt / EBITDAF ratio remains substantially unchanged post transaction. Contact expects the transaction to have no impact on its BBB credit rating from S&P.

## **Completion**

Completion of the sale of the AGS is subject to the fulfilment of certain conditions set out in the transaction agreements, including receipt of certain regulatory approvals.

The regulatory approvals include Ministerial consent under the Crown Minerals Act for the sale of the Ahuroa petroleum mining permit and change of operator, and Contact and GSNZ each obtaining required consents under the Overseas Investment Act 2005. Other conditions include GSNZ obtaining an IRD binding ruling as to the tax treatment of the main assets it is acquiring, and a third party taking up (or waiving) its limited entitlements to gas storage capacity in respect of the AGS.

Contact is targeting the satisfaction of these conditions and completion of the transaction by 30 June 2018.

## **On-going agreements**

Contact's need is for competitive storage services compatible with our requirements for flexible thermal generation, including the Stratford peaking plant. Contact has therefore entered into a 15 year agreement with GSNZ for the provision of gas storage services at a competitive annual fee. Contact also has the ability to extend the term of this agreement for further periods of five years at a time.

In addition, Contact will enter into an agreement with GSNZ to provide transitional services, such as operational support and IT services, for three months after completion of the sale transaction.



## **Background**

The AGS facility is a gas processing and compression plant and underground gas storage reservoirs located at Stratford in the Taranaki region of New Zealand. The AGS facility is currently used by Contact for gas injection, storage and withdrawal, and is capable of supporting the provision of storage services to other potential users. The storage capacity of the AGS is up to 18 petajoules, its gas injection capacity of up to 27 terajoules per day and gas extraction capacity of up to 45 terajoules per day.

In 2007, Contact acquired from Origin Energy the rights to develop a gas storage facility using the depleted Ahuroa gas field at a cost of \$164m. Between 2011 and 2017, Contact invested \$58m in the development of the AGS facility, providing the ability to inject pipeline specification gas.

Since taking over the operations of the facility in 2013, Contact has improved the integrity, reliability and costs of operation. The facility cost Contact \$6m p.a. to operate in FY17, compared to historical levels of >\$12m p.a.

## **About Gas Services New Zealand**

GSNZ provides operational services for First Gas and other customers. GSNZ operates one of New Zealand's largest gas networks, with 2,500 kilometres of high pressure gas transmission pipelines and around 4,800 kilometres of gas distribution pipelines in the North Island.

**Investor enquiries:** Matthew Forbes +64 21 072 8578



# Sale of the Ahuroa Gas Storage facility

Portfolio optimisation

Dennis Barnes, Chief Executive Officer  
Graham Cockroft, Chief Financial Officer

21 December 2017

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# Contact's strategy is to optimise the Customer and Generation businesses to deliver strong cash flows



## Customer

Will deliver value by providing customers with choice, certainty and control while reducing cost to serve and improving the customer experience through systems-enabled operational improvements



## Generation

A low cost, long life and flexible generation portfolio with a continuous improvement programme focusing on safety, spend, reliability and resource utilisation to improve the efficiency of our generation assets

Underpinned by a disciplined and transparent approach to operating and capital expenditure while continuing to investigate ways to optimise our portfolio of assets

# Executing our strategy – Transaction summary

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- » Contact has entered into an agreement to sell the Ahuroa Gas Storage facility (AGS) to Gas Services New Zealand (GSNZ) an associate of First Gas Limited (First Gas).
  - » GSNZ is a provider of operational services for First Gas and other customers. GSNZ operates one of New Zealand's largest gas networks, with 2,500 kilometres of high pressure gas transmission pipes and around 4,800 kilometres of gas distribution pipes in the North Island.
- » As part of the transaction, Contact has entered into a 15 year agreement for gas storage services with GSNZ at a level required to support Contact's generation portfolio. Contact will also provide certain transitional services for three months after completion of the sale.
- » The sale price of \$200 million, which is payable in cash at completion, will be subject to tax of approximately \$48 million. Contact will apply the net proceeds to the reduction of debt. The payment of tax will provide additional imputation credits, which could enable FY18 dividends to be distributed fully imputed to New Zealand shareholders.
- » To support potential new customers of AGS, GSNZ has committed to an expansion of AGS within approximately two years of completion of the sale of the transaction.
- » Until there are additional long term customers of the facility, S&P will capitalise the storage services payments. The S&P net debt / EBITDAF ratio remains substantially unchanged post transaction. Contact expects the transaction to have no impact on its BBB credit rating from S&P.

# Creating value for Contact shareholders through the sale of AGS

The AGS reservoir is larger than Contact's requirements and is capable of supporting storage services to other customers



**Monetising unused capacity**

- » By selling the last units that Contact uses from AGS, Contact is effectively selling the least valuable units of its current capacity to someone for whom the units will be the first and more valuable.



**GSNZ is a higher value owner**

- » GSNZ has a lower cost of capital than Contact.
- » GSNZ existing operations based in Taranaki present opportunities for operational synergies and enhanced gas market services.



**Reduction in gas storage costs**

- » Committed to an initial expansion of AGS, which reduces the cost per unit of storage.
- » Contact's effective share of operating costs will reduce as AGS signs up new customers.



**Independent owner of storage**

- » Without upstream or downstream interests, GSNZ is likely to be seen by potential new customers of AGS as a more independent counterparty than Contact.

# Contact retains access to competitive storage services compatible with thermal requirements

Flexible thermal generation is fundamental to the renewable New Zealand electricity market



## Flexible gas at reasonable cost

- » Gas storage makes large quantities of gas instantly available, for electricity generation, without the requirement to commit to long term take or pay arrangements with gas producers.



## Supporting renewables

- » New Zealand's renewable electricity supply peaks in summer while demand peaks in winter. The primary role of gas storage in the electricity market is to provide fuel for thermal generation when hydro-generation is below average.



## Economically delivering flexibility

- » The amount of flexible thermal fuel to provide a reliable electricity supply ranges between 40 and 50 PJ/annum.
- » Newer distributed and battery technologies cannot economically compete yet.



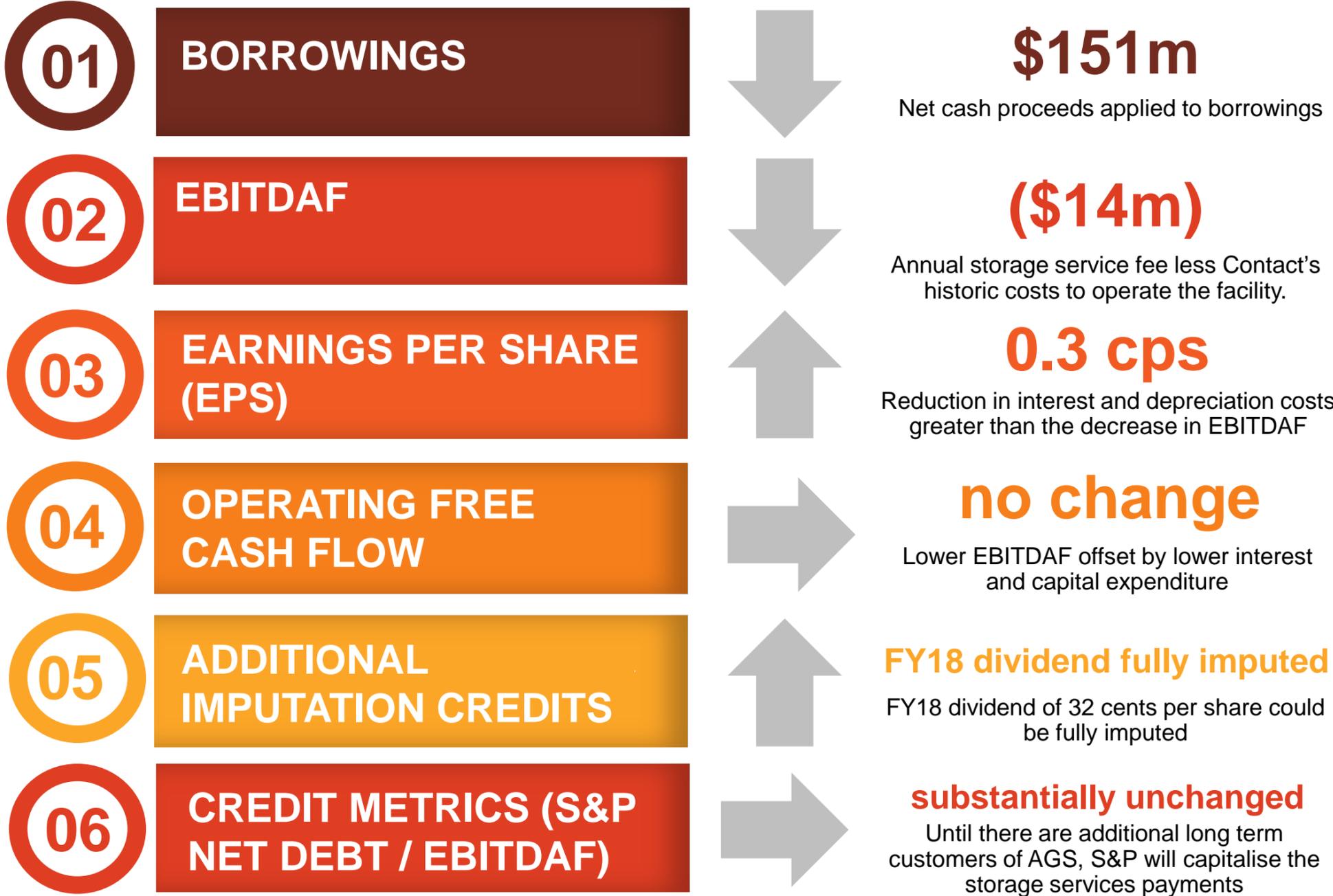
## 15 year gas storage agreement

- » Contact's own flexibility requirements from AGS for the operation of the Stratford peaking plant are contracted for 15 years.
- » Contact retains the ability to extend for further periods of 5 years at a time until 2050.

# Key transaction terms

	On Completion (targeted June 2018)	Post initial expansion (Completion +24 months)
Sale price	\$200m	
Net cash proceeds - after tax payable and \$1 million in transaction costs	\$151m	-
Accounting book value	\$184m	
Term of storage services	Initial term of 15 years, with the ability to extend for further periods of 5 years at a time until 2050	
AGS facility initial expansion	GSNZ to expand the facility within approximately 2 years of completion. Contact maintains its capacity rights following the expansion of the AGS facility.	
Facility capacity	27 TJ/day of injection and 45 TJ/day of extraction	65 TJ/day of injection and 65 TJ/day of extraction
Contact contracted capacity	75% of injection (up to 20.25 TJ/day) and extraction (up to 33.75 TJ/day)	69% of injection (up to 45 TJ/day) and extraction (up to 45 TJ/day)
Third party customers - Contact fee reduction	Contact's annual fee payable for gas storage services provided by GSNZ reduces where third party customers are contracted	
Contact annual fee payable to First Gas over an initial term of 15 years	\$20m + PPI	Less than \$20m + PPI if fully contracted

# Key financial impacts



**Economics of the transaction expected to improve with Contact's foundation rights maintained**

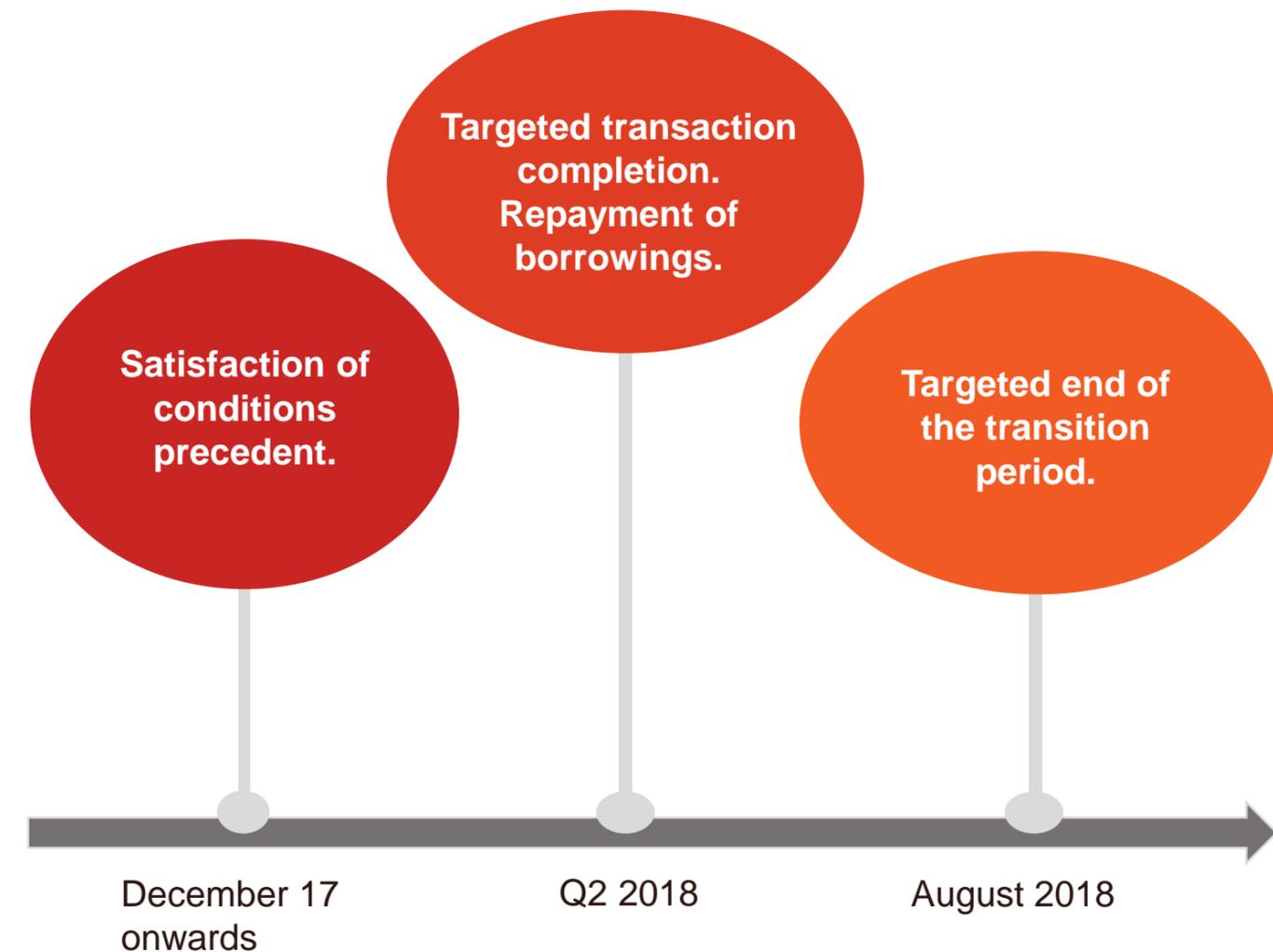
- » AGS initial expansion will facilitate further third party sales and potentially trigger a change in the S&P treatment of the Contact storage agreement
- » AGS expansion increases plant resilience and availability
- » Fee reduction mechanism where third party customers are added reduces cost to Contact of gas storage services
- » Potential for further expansions

# Conditions precedent and transaction timeline

## Limited conditions precedent

- 01** Ministerial consent for the transfer of the petroleum mining permit and change of operator
- 02** Overseas Investment Office (OIO) consent for GSNZ to purchase AGS
- 03** OIO consent for Contact to enter into the gas storage services agreement
- 04** GSNZ to obtain an Inland Revenue binding ruling on tax treatment of AGS
- 05** Agreement from a third party to take up or waive its entitlements to limited gas storage capacity

Contact is targeting transaction completion by the end of FY18



# Commercialising AGS - Available capacity at AGS for new customers

25% of the capacity of AGS is available for long term contracting. This will increase post expansion.

Gas storage services	Current available capacity for additional customers	Post initial expansion (Completion +24 months)
Storage capacity	4.5 PJ	4.5 PJ
Injection capacity	6.75 TJ/day of injection	20 TJ/day of injection
Extraction capacity	11.25 TJ/day of extraction	20 TJ/day of extraction



# AGS history

- » In December 2007, in conjunction with Origin Energy's acquisition of the New Zealand assets of Swift Energy, Contact acquired from Origin the rights to develop an underground gas storage facility using the depleted Ahuroa gas field. The cost of the acquisition was \$164m, including 4 PJ of cushion gas.
- » Between 2011 and 2017, Contact invested \$58m in the development of the AGS facility, providing the ability to inject pipeline specification gas.
- » Origin was originally the operator of the AGS facility and also provided reservoir management services for Contact. When Origin sold its onshore NZ assets to New Zealand Energy Company (NZEC) in 2013, Contact entered into agreements for operational services with NZEC.
- » Contact has improved the integrity, reliability and costs of operation since 2013. The facility cost Contact \$6m p.a. to operate in FY17, compared to historical levels of >\$12m p.a.

