TRANSPOWER

D.17

Interim Report 2019/20

Introduction

On behalf of the Board and Management, we are pleased to share Transpower New Zealand's financial results for the six months ending 31 December 2019.

The Board is pleased with the solid first-half results for the six months to December 2019, in terms of financial performance, delivery of the capital programme and steady returns to shareholders.

Net profit after tax, before net changes in the fair value of financial instruments, was $105.2 million, in line with the previous period's result of $105.3 million.

Transmission revenue declined 1.3% to $482.7 million (2018: $489.2 million) mainly due to pricing changes while operating expenses at $135.1 million, were down 5.7% compared to the previous period (2018: $143.3 million).

Capital expenditure was $173.4 million, up 33 per cent from the same time last year (2018: $130.4 million) and in line with Transpower's approved capital programme.

An interim dividend of 6 cents/share or $66 million has been declared, representing 40 per cent of the expected full-year dividend forecast in Transpower's 2019/20 Statement of Corporate Intent.

We remain well on track to deliver on the majority of the targets set in our Statement of Corporate Intent, however two of our Health and Safety targets, namely TRIFR and HIPFR look challenging, as does our staff engagement. In addition, we expect to not meet our HVDC availability target due to the planned outage for maintenance during the remainder of FY20.

Ensuring the health, safety and wellbeing of our workforce is a particular focus for the Board and Management. We are continuing to work closely with our service providers to deliver appropriate intervention programmes to address our injury and high potential incident frequency rates. We have moved to a new form of engagement survey that will support a process of continuous feedback, listening and action planning.

The Commerce Commission continues to investigate breaches under the Individual Price-Quality Path (IPP) regime under Part 4 of the Commerce Act. The Commission issued a warning letter in respect of the 15/16 and 16/17 financial years and is investigating breaches that occurred in 17/18 and subsequent years in the five-year regulatory period through to 30 June 2020 to see whether further enforcement action is warranted.

The Commission has acknowledged that we largely managed our network in accordance with good electricity industry practice and we have already taken steps to mitigate against the issues raised. We will continue to work alongside the Commission and our customers during these investigations to seek ways to improve our operational practices.

The first half of the financial year brought some new opportunities and some unexpected challenges for Transpower but the organisation is on track with its capital works and maintenance programme.

The agreement with Contact and Meridian to commence further work on the Clutha-Upper Waitaki lines in response to Rio Tinto's announcement of an review of their New Zealand operations and the loss of nine towers from the Roxburgh-Islington line following the flooding of the Rangitata River have led to some change in our programme work.

Regardless, Transpower has demonstrated its ability to respond quickly to challenges that can arise unexpectedly and seize new opportunities while maintaining service levels to customers and communities.

We continue to work toward a strong close of the current regulatory period and the commencement of the new regulatory period from July 2020.

Over the past six months, we have been exploring the future expectations of the grid to meet the needs of New Zealand as we move further toward the Government's goal of a net zero carbon economy. We are committed to doing our part to help the Government achieve its climate change goals and our Te Mauri Hiko – Energy Futures programme of research and industry engagement has continued with some new work to be released in the next few months.

PIP DUNPHY
CHAIR

ALISON ANDREW
CHIEF EXECUTIVE

Statement of comprehensive income

For the six months ended 31 December 2019

		GROUP	
	NOTES	**2019 UNAUDITED $M**	**2018 UNAUDITED $M**
Operating revenue	2	510.3	516.2
Operating expenses	3	135.1	143.3
Earnings before interest, tax, depreciation, amortisation, asset write-offs, impairment and changes in the fair value of financial instruments		375.2	372.9
Depreciation, amortisation, write-offs and impairment	5, 6	137.1	132.4
Net interest expenses	4, 6	91.8	94.0
Earnings before changes in the fair value of financial instruments and tax		146.3	146.5
Gain (loss) in the fair value of financial instruments	10	56.7	34.6
Earnings before tax		203.0	181.1
Income tax expense		57.0	50.9
NET PROFIT		146.0	130.2
Attributable to:			
Non-controlling interest		(0.2)	0.3
Owners of the parent		146.2	129.9
Other comprehensive income (expense)	10	3.0	1.1
Attributable to:			
Non-controlling interest		-	-
Owners of the parent		3.0	1.1
Total comprehensive income		149.0	131.3
Attributable to:			
Non-controlling interest		(0.2)	0.3
Owners of the parent		149.2	131.0
Reconciliation of net profit specifying the net impact of fair value movements			
Earnings before changes in the fair value of financial instruments and tax		146.3	146.5
Income tax expense excluding changes in the fair value of financial instruments		41.1	41.2
Earnings before net changes in fair values of financial instruments	1	105.2	105.3
Gain (loss) in the fair value of financial instruments		56.7	34.6
Income tax credit (expense) on changes in the fair value of financial instruments		(15.9)	(9.7)
NET PROFIT		146.0	130.2

These statements are to be read in conjunction with the accompanying notes.

Statement of financial position

As at 31 December 2019

	NOTES	GROUP 2019 UNAUDITED 31 DECEMBER $M	2019 AUDITED 30 JUNE $M
ASSETS EMPLOYED			
Cash and cash equivalents		194.8	156.5
Investments - short-term		109.0	99.9
Trade receivables and other assets	8	127.5	136.1
Derivatives and hedge commitment in gain	8	317.6	321.2
NZPCL investment	8	88.8	85.7
Property, plant and equipment	5	4,633.3	4,621.8
Intangibles - long-term		373.5	372.9
Right-of-use asset	6	124.1	-
Capital work in progress	5	187.2	138.3
TOTAL ASSETS EMPLOYED		6,155.8	5,932.4
FUNDS EMPLOYED			
Liabilities			
Cash and cash equivalents		-	0.3
Trade and other payables	8	95.7	97.2
Current tax liability		10.8	24.0
Deferred income		154.5	129.8
Derivatives and hedge commitment in loss	8	164.3	213.4
Provisions	8	50.4	63.5
Debt	7	3,320.4	3,227.4
NZPCL debt	8	90.1	86.7
Lease liabilities	6	102.2	-
Deferred tax		476.9	449.6
Total liabilities		4,465.3	4,291.9
Equity			
Capital		1,200.0	1,200.0
Accumulated surplus		480.4	441.3
Cash flow hedge reserve		11.1	-
Non-controlling interest		(1.0)	(0.8)
Total equity		1,690.5	1,640.5
TOTAL FUNDS EMPLOYED		6,155.8	5,932.4

The board of directors of Transpower New Zealand Limited authorised these financial statements for issue on 28 February 2020.
For, and on behalf of, the board.

PIP DUNPHY
CHAIR

KATHY MEADS
CHAIR AUDIT & FINANCE COMMITTEE

These statements are to be read in conjunction with the accompanying notes.

Statement of changes in equity

For the six months ended 31 December 2019

2019						GROUP UNAUDITED
	ORDINARY SHARES $M	RETAINED EARNINGS $M	CASH FLOW HEDGE RESERVE $M	OWNERS OF THE PARENT $M	NON-CONTROLLING INTEREST $M	TOTAL $M
Equity at 1 July 2019	1,200.0	441.3	-	1,641.3	(0.8)	1,640.5
Profit for the period	-	146.2	-	146.2	(0.2)	146.0
Other comprehensive income	-	(8.1)	11.1	3.0	-	3.0
Total comprehensive income	-	138.1	11.1	149.2	(0.2)	149.0
Dividends	-	(99.0)	-	(99.0)	-	(99.0)
TOTAL EQUITY AT 31 DECEMBER 2019	1,200.0	480.4	11.1	1,691.5	(1.0)	1,690.5

2018						GROUP UNAUDITED
	ORDINARY SHARES $M	RETAINED EARNINGS $M	CASH FLOW HEDGE RESERVE $M	OWNERS OF THE PARENT $M	NON-CONTROLLING INTEREST $M	TOTAL $M
Equity at 1 July 2018	1,200.0	356.8	-	1,556.8	(1.1)	1,555.7
Profit for the period	-	129.9	-	129.9	0.3	130.2
Other comprehensive income	-	1.1	-	1.1	-	1.1
Total comprehensive income	-	131.0	-	131.0	0.3	131.3
Dividends	-	(99.0)	-	(99.0)	-	(99.0)
TOTAL EQUITY AT 31 DECEMBER 2018	1,200.0	388.8	-	1,588.8	(0.8)	1,588.0

These statements are to be read in conjunction with the accompanying notes.

Cash flow statement

For the six months ended 31 December 2019

	GROUP	
	2019 UNAUDITED $M	**2018** UNAUDITED $M
CASH FLOW FROM OPERATIONS		
Receipts from customers	521.0	518.2
Interest received	2.8	3.4
Payments to suppliers and employees	(122.6)	(157.9)
Tax payments	(44.2)	(47.6)
Interest paid	(92.5)	(99.2)
Net cash inflows (outflows) from operations	264.5	216.9
CASH FLOW FROM INVESTMENTS		
Sale of property, plant and equipment	1.6	6.7
Sale of short-term investments	24.7	96.0
Purchase of property, plant and equipment and intangibles	(221.5)	(147.8)
Purchase of short-term investments	(34.0)	(43.4)
Net cash inflows (outflows) from investments	(229.2)	(88.5)
CASH FLOW FROM FINANCING		
Proceeds from bonds, term debt and commercial paper	835.1	273.1
Dividends paid	(99.0)	(99.0)
Payment of principal portion of lease liabilities	(7.9)	-
Repayment of bonds, term debt and commercial paper	(724.9)	(325.0)
Net cash inflows (outflows) from financing	3.3	(150.9)
Net increase (decrease) in cash held	38.6	(22.5)
Opening balance brought forward	156.2	75.0
Closing net cash carried forward	194.8	52.5
Closing net cash carried forward comprises:		
Cash and on-call deposits	59.7	52.5
Short-term deposits with original maturity less than three months	135.1	-

These statements are to be read in conjunction with the accompanying notes.

Cash flow statement reconciliation

Reconciliation of net profit with net cash flow from operations
For the six months ended 31 December 2019

	GROUP	
	2019 UNAUDITED $M	**2018 UNAUDITED $M**
Net profit	146.0	130.2
Add (deduct) non-cash items:		
Change in fair value of financial instruments	(56.8)	(34.8)
Depreciation, amortisation and write-offs	137.1	132.4
Deferred tax	26.1	20.4
Capitalised interest	(4.7)	(3.2)
Movements in working capital items:		
Increase in trade and other receivables	(12.3)	(13.3)
Increase in trade and other payables, interest payable and deferred income	45.4	4.3
Decrease in taxation payable	(13.2)	(16.6)
Decrease in provisions	(3.1)	(2.5)
NET CASH FLOW FROM OPERATIONS	264.5	216.9

These statements are to be read in conjunction with the accompanying notes.

Notes to the financial statements

1. Transpower Group information

Reporting entity and statutory base

Transpower New Zealand Limited (Transpower) is a State-Owned-Enterprise registered in New Zealand under the Companies Act 1993. The financial statements are in New Zealand dollars and are of Transpower and its subsidiaries (together, the Group).

The Group is the owner and operator of New Zealand's national electricity grid. The Group is a for-profit entity in accordance with XRB A1 Application of the Accounting Standards Framework.

Basis of preparation

The financial statements included in this half-yearly report have been prepared in compliance with NZ IAS 34 Interim Financial Reporting and IAS 34 Interim Financial Reporting and should be read in conjunction with the 2018/19 audited annual financial statements.

The accounting policies used in preparation of these financial statements are consistent with those used in preparation of the 2018/19 audited annual financial statements with the exception of one new accounting standard adopted NZ IFRS 16 Leases. The 2018/19 audited annual financial statements can be viewed at www.transpower.co.nz.

Transpower's operations are not considered seasonal or cyclical in nature.

Where necessary, certain comparative information has been reclassified to conform to changes in presentation in the current period.

New standards adopted during the period

During the period, Transpower adopted NZ IFRS 16 Leases. NZ IFRS 16 supersedes NZ IAS 17 Leases and sets out the principles for the recognition, measurement, presentation and disclosure of leases. It requires lessees to recognise most leases on the balance sheet. Accordingly, the profit or loss impact is a decrease in leasehold expenditure and an increase in depreciation expense and imputed interest.

Transpower adopted NZ IFRS 16 using the modified retrospective method of adoption with the date of initial application of 1 July 2019. Under this method, the cumulative effect will flow through retained earnings at the date of initial application.

Upon adoption of NZ IFRS 16, Transpower applied a single recognition and measurement approach for all leases except for short-term leases and leases of low-value assets. Transpower applies the short-term lease recognition exemption to its short-term leases (i.e. those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). Transpower also applies the lease of low-value assets recognition exemption to leases of office equipment that are considered to be low value. Lease payments for these leases are recognised as an expense on a straight-line basis over the lease term.

The effect of adopting NZ IFRS 16 as at 1 July 2019 (increase/(decrease)) is, as follows:

	$M
Assets	
Right-of-use assets	129.1
Property, plant and equipment	-
Prepayments	(23.0)
Total assets	106.1
Liabilities	
Lease Liabilities	106.1
Deferred tax liabilities	-
Trade and other payables	-
Total liabilities	106.1
Total adjustment on equity	
Retained earnings	-
Non-controlling interest	-
TOTAL EQUITY	-

The lease liabilities as at 1 July 2019 can be reconciled to the operating lease commitments as of 30 June 2019, as follows:

	$M
Operating lease commitments as at 30 June 2019	112.2
Weighted average incremental borrowing rate as at 1 July 2019	3.48%
Discounted operating lease commitments as at 1 July 2019	83.9
Less:	
Commitments relating to short-term leases	-
Commitment relating to leases not containing an asset	(20.8)
Commitments relating to leases of low-value assets	-
Add:	
Lease payments relating to extensions deemed reasonably certain	43.0
Lease liabilities as at 1 July 2019	106.1

Measurement basis

The measurement basis adopted in the preparation of these financial statements is historical cost except as modified for certain investments, held-for-sale assets, financial assets and financial liabilities.

Transpower discloses an alternative measure of profit, which is earnings before net changes in fair values of financial instruments. Transpower discloses this information as it provides a different measure of underlying performance to the IFRS-mandated profit measures, which are also disclosed. The Directors consider that this additional profit measure is useful additional information for users of the financial statements and is a measure that Directors consider when setting the level of dividend payments to the shareholder. Transpower has consistently reported an alternative profit on this basis since the adoption of IFRS.

New standards not yet adopted

Transpower has elected not to early adopt any standards (or revisions to standards), considered to be relevant to the financial statements, but not yet effective.

2. Operating revenue

For the six months ended 31 December 2019

	GROUP	
	2019 UNAUDITED $M	**2018** UNAUDITED $M
Transmission revenue		
HVAC interconnection	327.5	340.1
HVAC connection	64.8	64.7
EV (rebate) charge - HVAC	(1.5)	(10.6)
HVDC	74.3	75.6
EV (rebate) charge - HVDC	(1.9)	0.5
Other regulated transmission	2.4	2.2
Customer investment contracts	14.1	13.4
Undergrounding and transmission realignment	2.2	2.3
Other transmission	0.8	1.0
	482.7	489.2
Other revenue		
System operator	20.8	20.6
Other	6.8	6.4
	27.6	27.0
Total operating revenue	510.3	516.2

Government-related transactions
Transpower, being a State-Owned-Enterprise, transacts with other government-related entities.
The most significant transactions and balances (greater than $15 million) are as follows:

	2019 $M	**2018** $M
Meridian Energy Limited - revenue	56.6	59.6
Electricity Authority - revenue	21.0	21.0
	77.6	80.6

Description

Transmission revenue
Transmission revenue consists of charges for the transmission of electricity from the point of generation to the point of supply, being high voltage alternating current (HVAC) interconnection, connection and high voltage direct current (HVDC).

Customer investment contracts are contracts entered into with customers to build grid connection assets. Transpower recognises this revenue over the life of the asset.

Undergrounding and transmission realignment contracts are contracts entered into with third parties to underground and/or realign certain transmission line assets. The revenue is recognised based on the revenue source. If the revenue is received from central or local government or their agencies, then the revenue is recognised over the life of the related transmission assets according to NZ IAS 20. If revenue is received from non-government parties, then it is recognised once the related assets are commissioned with the related assets written off.

Other revenue
System operator – System operator income relates to payments received for the provision of real-time services to ensure the short-term security of the New Zealand electricity system.

3. Operating expenses

For the six months ended 31 December 2019

	GROUP	
	2019 UNAUDITED $M	**2018** UNAUDITED $M
Grid maintenance		
HVAC substations maintenance	19.9	21.9
HVDC substations and cables maintenance	4.5	4.3
HVAC lines maintenance	19.6	18.6
HVDC lines maintenance	0.8	0.5
Transmission-related rates	3.5	3.8
Other	3.3	3.5
	51.6	52.6
IST maintenance and operations		
Support and maintenance	4.1	4.4
Outsourced services	5.5	7.1
Licenses	4.5	4.5
Other IST	1.3	3.8
	15.4	19.8
Other operating expenses		
Investigations	7.1	6.7
Ancillary service costs	1.8	2.2
Employee benefits	57.0	56.3
Capitalised salary costs	(13.3)	(11.2)
Salary transferred to investigations	(2.6)	(2.9)
Industry levies	5.0	5.0
Insurance	2.3	2.1
Other business support costs	10.8	12.7
	68.1	70.9
Total operating expenses	135.1	143.3

Description

Maintenance includes inspection, servicing and repair costs.

Other grid maintenance expenses include maintenance support, communication system and training for service providers and third parties.

Investigations includes work that the Group conducts prior to the commencement of a capital project, updates to maintenance standards and demand-response costs.

Other business support costs include such items as lease expenses relating to short-term leases and low-value assets, legal fees, office equipment, communications, vehicles, travel, consultants and contractors.

In the December 2018 comparatives, the Group had lease payments of $6.2 million in Other IST and Other business support costs.

Related disclosures

	GROUP	
	2019 UNAUDITED $000	**2018** UNAUDITED $000
Fees paid to external auditor		
Audit of financial statements		
Audit and reviews of financial statements	269	254
Other services		
Training courses	25	54
Trust deed requirements	11	11
Remuneration benchmarking report	5	6
Financial model assurance	8	21
Other assurance	59	-
	108	92
Total fees paid to external auditor	377	346

4. Net interest expenses

For the six months ended 31 December 2019

	GROUP	
	2019 UNAUDITED $M	**2018** UNAUDITED $M
Interest revenue		
Interest received	2.8	3.4
	2.8	3.4
Interest expenses		
Interest paid and associated fees	93.1	97.0
Capitalised interest	(4.7)	(3.2)
Imputed interest	6.2	3.6
	94.6	97.4
Total net interest expenses	91.8	94.0

Description

Capitalised interest is based on Transpower's forecast weighted average cost of borrowing, which, for the six months to December 2019, was 6.47% (6 months to December 2018: 6.59%).

Imputed interest includes interest arising on deferred income, the unwind of the discount of future cash flows related to provisions, and interest on lease liabilities.

5. Non-current assets

	HVAC TRANSMISSION LINES $M	HVDC TRANSMISSION LINES $M	HVAC SUBSTATIONS $M	HVDC SUBSTATIONS AND SUBMARINE CABLES $M	COMMUNICATIONS $M	ADMINISTRATION ASSETS $M	TOTAL PROPERTY, PLANT AND EQUIPMENT $M	CAPITAL WORK IN PROGRESS $M
								GROUP
At 31 December 2019								
Cost	2,716.2	148.2	2,659.7	875.1	390.2	194.6	6,984.0	187.2
Accumulated depreciation	(736.5)	(58.4)	(826.2)	(380.4)	(221.7)	(127.5)	(2,350.7)	-
Net book value	1,979.7	89.8	1,833.5	494.7	168.5	67.1	4,633.3	187.2
31 December 2019 reconciliation								
Opening net book value (1 July 2019)	1,981.5	91.8	1,790.3	510.8	175.5	71.9	4,621.8	138.3
Additions / transfers	33.1	-	79.9	2.6	7.8	1.1	124.5	48.9
Disposals / transfers	-	-	(1.5)	(0.1)	(0.1)	-	(1.7)	-
Depreciation	(34.9)	(2.0)	(35.2)	(18.6)	(14.7)	(5.9)	(111.3)	-
Closing net book value	1,979.7	89.8	1,833.5	494.7	168.5	67.1	4,633.3	187.2
At 30 June 2019								
Cost	2,683.9	148.2	2,583.1	873.0	382.5	193.6	6,864.3	138.3
Accumulated depreciation	(702.4)	(56.4)	(792.8)	(362.2)	(207.0)	(121.7)	(2,242.5)	-
Net book value	1,981.5	91.8	1,790.3	510.8	175.5	71.9	4,621.8	138.3
30 June 2019 reconciliation								
Opening net book value (1 July 2018)	1,958.8	96.7	1,765.1	542.4	177.6	74.4	4,615.0	75.0
Additions / transfers	95.1	1.9	102.0	5.0	27.2	9.2	240.4	328.9
Disposals / transfers	(4.3)	(2.9)	(5.3)	-	(0.6)	(0.1)	(13.2)	(265.6)
Impairment	-	-	-	-	-	-	-	-
Depreciation	(68.1)	(3.9)	(71.5)	(36.6)	(28.7)	(11.6)	(220.4)	-
Closing net book value	1,981.5	91.8	1,790.3	510.8	175.5	71.9	4,621.8	138.3
At 31 December 2018								
Cost	2,606.6	147.5	2,526.4	870.0	367.4	186.8	6,704.7	135.6
Accumulated depreciation	(669.0)	(54.6)	(760.6)	(343.8)	(199.4)	(116.9)	(2,144.3)	-
Net book value	1,937.6	92.9	1,765.8	526.2	168.0	69.9	4,560.4	135.6
31 December 2018 reconciliation								
Opening net book value (1 July 2018)	1,958.8	96.7	1,765.1	542.4	177.6	74.4	4,615.0	75.0
Additions / transfers	19.8	0.5	43.8	2.0	5.1	2.8	74.0	60.6
Disposals / transfers	(7.6)	(2.3)	(7.1)	-	(0.7)	(0.8)	(18.5)	-
Depreciation	(33.4)	(2.0)	(36.0)	(18.2)	(14.0)	(6.5)	(110.1)	-
Closing net book value	1,937.6	92.9	1,765.8	526.2	168.0	69.9	4,560.4	135.6

Description

Property, plant and equipment
Administration assets include computer hardware, plant, equipment, furniture and motor vehicles.

Key judgements

Transpower has exercised judgement in the following areas:

1) Determining the useful life of property, plant and equipment and finite life intangible assets. Transpower uses assistance from independent engineers. For transmission line assets, a determining factor in the life assumption is proximity to the coast.
2) Whether or not an item is capital in nature and the appropriate component level of asset at which to depreciate.
3) Determining the appropriate time to commission an asset and commence depreciation.
4) Whether there are any regulated assets that ought to be impaired.

6. Leases

			GROUP
	PROPERTY AND IT DATA CENTRES $M	FIBRE COMMUNICATION NETWORK $M	TOTAL $M
Right-of-use assets			
31 December 2019 reconciliation			
Opening net book value (1 July 2019)	-	-	-
Effect of adoption of IFRS 16	67.0	62.1	129.1
Additions	-	-	-
Depreciation	(2.5)	(2.5)	(5.0)
Closing net book value	64.5	59.6	124.1

	GROUP
	$M
Lease liabilities	
31 December 2019 reconciliation	
Opening balance (1 July 2019)	-
Effect of adoption of IFRS 16	106.1
Additions	-
Accretion of interest	1.8
Payments	(5.7)
Closing balance	102.2
Current	7.1
Non-current	95.1

Description

The Group's leases primarily relate to the leasing of fibre optic cables for Transpower's communication network and property leases for office buildings and IT data centres.

Accounting Policies

Lease liabilities

Lease liabilities are recognised based on the present value of the remaining lease payments, including lease renewals that are deemed reasonably certain to be exercised. The Group uses the incremental borrowing rate at the lease commencement date to calculate the present value of lease payments.

Lease liabilities will decrease over time as lease payments are made and increase with an imputed interest expense being recognised. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term or a change in the in-substance fixed lease payments.

Right-of-use assets

The Group recognises right-of-use assets at the commencement date of the lease (i.e. the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurements of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, adjusted for any remaining prepaid lease payments. The right-of-use assets are depreciated on a straight-line basis over the shorter of their estimated useful life and the lease term.

Key judgements

Transpower has exercised judgement in the following areas:

1) Determination of whether or not a lease exists through assessment of contractual arrangements;
2) Where the contract contains options to extend or terminate the lease, consideration of the likelihood of exercising the options based on past practice; and
3) Use of a single discount rate to a portfolio of leases with reasonably similar characteristics.

Related Disclosure

The following are the amounts recognised in profit or loss:

For the six months ended 31 December 2019	2019 UNAUDITED $M
Depreciation expense of right-of-use assets	5.0
Interest expenses on lease liabilities	1.8
Expense relating to short-term leases and leases of low-value asset (included in operating expenses)	1.4
Total amount recognised in profit or loss	8.2

The group had total cash outflow for lease payments of $6.8 million in 2020 (2019: $6.2 million).

7. Debt

	GROUP	
	2019 **UNAUDITED** **31 DECEMBER** **$M**	**2019** **AUDITED** **30 JUNE** **$M**
Current debt		
Short-term debt	209.6	74.8
Current portion of long-term debt	349.8	722.9
Total current debt	559.4	797.7
Long-term debt		
Bonds	1,152.2	1,269.3
Domestic Bank Term	100.1	100.1
Euro Medium Term Notes	78.8	78.0
Swiss Medium Term Notes	190.2	-
Australian Medium Term Notes	529.8	536.5
U.S. Private Placement Notes	1,059.7	1,168.7
	3,110.8	3,152.6
Less current portion of long-term debt	(349.8)	(722.9)
Total long-term debt	2,761.0	2,429.7
Total debt	3,320.4	3,227.4

Description
Debt is reported at fair value and therefore reflects value movements due to interest rate and exchange rate fluctuations.

Debt issuances and repayments during the period
During the six months to 31 December 2019, Transpower repaid the following debt:
NZD 200m of bonds, maturing 6 September 2019 with a coupon of 4.65%;
NZD 50m of bonds, maturing 12 November 2019 with a coupon of 7.19%; and
USD 75m ($123.4m NZD equivalent) of USPP, maturing 27 September 2019 with a coupon of 5.74%.

During the six months to 31 December 2019, Transpower issued the following debt:
NZD 150m of bonds on 4 September 2019 with a coupon of 1.74%; and
CHF 125m ($196.8m NZD equivalent) of bonds on 16 December 2019 with a coupon of 0.02%.

Key judgements
A key judgement has been made in relation to the fair values of debt and derivatives. Fair values are determined by discounting cash flows based on the relevant yield curve. The yield curve is adjusted to reflect the credit risk of the counterparty to the transaction or the credit risk of Transpower. These valuations are considered level two in the IFRS three-level valuation hierarchy.

Debt at face value as amended by foreign exchange derivatives

	GROUP	
	2019 UNAUDITED 31 DECEMBER $M	**2019 AUDITED 30 JUNE $M**
Short-term debt	209.3	74.7
Current portion of long-term debt	323.1	696.5
Total current debt	532.4	771.2
Bonds	1,075.0	1,175.0
Domestic Bank Term	100.0	100.0
Euro Medium Term Notes	73.1	73.1
Swiss Medium Term Notes	196.8	-
Australian Medium Term Notes	506.9	506.9
U.S. Private Placement Notes	889.9	1,013.2
	2,841.7	2,868.2
Less current portion of debt	(323.1)	(696.5)
Total long-term debt	2,518.6	2,171.7
Total debt	3,051.0	2,942.9

8. Statement of financial position short-term long-term split

Transpower has elected to present its statement of financial position based on liquidity in accordance with NZ IAS 1. The table below presents the short-term and long-term assets and liabilities where this distinction is not otherwise apparent in the financial statements.

At 31 December 2019						GROUP
	SHORT-TERM ASSET $M	LONG-TERM ASSET $M	TOTAL ASSET $M	SHORT-TERM (LIABILITY) $M	LONG-TERM (LIABILITY) $M	TOTAL (LIABILITY) $M
Trade receivables, payables and other	124.2	3.3	127.5	(95.1)	(0.6)	(95.7)
Derivatives and hedge commitment	53.3	264.3	317.6	(72.9)	(91.4)	(164.3)
NZPCL investment/debt	-	88.8	88.8	-	(90.1)	(90.1)
Provisions	-	-	-	(9.9)	(40.5)	(50.4)

At 30 June 2019						GROUP
	SHORT-TERM ASSET $M	LONG-TERM ASSET $M	TOTAL ASSET $M	SHORT-TERM (LIABILITY) $M	LONG-TERM (LIABILITY) $M	TOTAL (LIABILITY) $M
Trade receivables, payables and other	113.5	22.6	136.1	(96.6)	(0.6)	(97.2)
Derivatives and hedge commitment	58.2	263.0	321.2	(119.4)	(94.0)	(213.4)
NZPCL investment/debt	-	85.7	85.7	-	(86.7)	(86.7)
Provisions	-	-	-	(23.8)	(39.7)	(63.5)

9. Segment reporting

For the six months ended 31 December 2019

The Group has two segments – transmission and system operator. The segments reported for 31 December 2019 have not changed from 30 June 2019.

- **Transmission** – the transmission of electricity from the point of generation to the point of connection.
- **System operator** – operates the electricity market to dispatch generation to ensure the short-term security of the New Zealand electricity system.

Both segments have external revenue derived from New Zealand customers and assets based in New Zealand. The Group has no other reportable segments.

The material portion of **Other** is made up of Risk Reinsurance Limited, which was established in 2011 to provide insurance services to the Group.

Segment results are determined based on information provided to the Chief Operating Decision Maker. They are calculated using the avoidable cost allocation methodology (ACAM).

	TRANSMISSION		SYSTEM OPERATOR		OTHER		ADJUSTMENTS		TOTAL	
	UNAUDITED 2019 $M	UNAUDITED 2018 $M	UNAUDITED 2019 $M	UNAUDITED 2018 $M	UNAUDITED 2019 $M	UNAUDITED 2018 $M	UNAUDITED 2019 $M	UNAUDITED 2018 $M	UNAUDITED 2019 $M	UNAUDITED 2018 $M
External revenue	483.0	486.1	20.8	20.6	6.5	6.1	-	3.4	510.3	516.2

10. Change in fair value of financial instruments

For the six months ended 31 December 2019

	GROUP	
	2019 UNAUDITED $M	**2018** UNAUDITED $M
Fair value through profit or loss		
Accounting hedges		
Foreign exchange forward contracts - hedge accounted	-	(0.9)
Hedge commitment	-	0.9
	-	-
Other		
Foreign debt	14.7	9.4
Cross currency interest rate swaps	(4.3)	(15.7)
NZD interest rate swaps	34.2	36.0
Investments	(0.2)	0.3
NZD debt	12.3	4.6
	56.7	34.6
Total fair value gain (loss)	56.7	34.6

Fair value through other comprehensive income		
Credit spread on debt		
Foreign debt	(10.3)	6.5
NZD debt	(0.9)	(5.0)
Gross fair value gain (loss)	(11.2)	1.5
Less income tax credit (expense)	3.1	(0.4)
	(8.1)	1.1
Cash flow hedging		
Interest risk	15.4	-
Gross fair value gain (loss)	15.4	-
Less income tax credit (expense)	(4.3)	-
	11.1	-
Total other comprehensive income (expenses)	3.0	1.1

Description

The Group experiences changes in fair value through movements in underlying interest rates, exchange rates and credit spread on debt and derivatives. The Group generally seeks to fix interest rates to provide certainty of interest rate costs during regulatory control periods. This means that, prima facie, a decrease in market interest rates will result in the Group sustaining fair value losses, and conversely, an increase in market interest rates will result in fair value gains.

The fair value of debt and derivatives is determined by converting currency exposures and discounting cash flows based on the relevant yield curve. The yield curve is adjusted to reflect the credit risk of the counterparty to the transaction or the credit risk of Transpower. These valuations are considered level two in the IFRS three-level valuation hierarchy. There have been no movements between levels during the period.

Changes in fair value of financial instruments are separately disclosed as fair value changes through profit and loss, or through other comprehensive income. The fair value change through other comprehensive income comprises fair value changes resulting from credit spread changes on the Group's issued debt and the effective portion of fair value changes on derivatives designated as cash flow hedges for accounting.

Cash flow hedges

During the period, the Group has designated certain interest rate swaps into the cash flow hedge accounting relationships, which align interest rate exposures to the Regulatory Control Period. The Group uses the hypothetical derivative method to measure hedge accounting effectiveness and compares the changes in the fair value of the hedging instruments against the changes in fair value of the hedged item attributable to hedged risk. To the extent these hedges are effective, the change in fair value of the hedging instrument is recognised in other comprehensive income in the Cash Flow Hedge Reserve within Equity, while the change in fair value on the ineffective portion is recognised immediately in the statement of profit or loss. The cash flow hedge reserve is adjusted to the lower of the cumulative gain or loss on the hedging instrument and the cumulative change in fair value of the hedged item. Hedge ineffectiveness in the cash flow hedge accounting relationship can arise from movements in credit risk on hedging instrument counterparties.

Fair values in statement of financial position

For cash and cash equivalents, accounts payable and receivables, fair values are materially similar to their cost due to the short-term nature of these items.

The following items are recorded at fair value:

Asset (liability)		GROUP
	2019 UNAUDITED 31 DECEMBER $M	2019 AUDITED 30 JUNE $M
Investments	109.0	99.9
Derivatives and hedge commitment in gain	317.6	321.2
NZPCL investment	88.8	85.7
Derivatives and hedge commitment in loss	(164.3)	(213.4)
Debt	(3,320.4)	(3,227.4)
NZPCL debt	(90.1)	(86.7)

11. Contingencies

(i) Guarantees

New Zealand Power Caymans Limited (NZPCL)

In November 2009, the Group partially terminated the 2003 cross-border lease in respect of the majority of the HVAC transmission assets in the South Island. As a result of the partial termination, Transpower has consolidated a special-purpose vehicle, NZPCL.

NZPCL has a USD deposit with a financial institution and a USD loan from another financial institution. The cash flows from the deposit and loan offset. No consideration was transferred. The loan to NZPCL is guaranteed by Transpower.

The substance of the transaction is such that Transpower rather than the non-controlling interest would be responsible for any shortfall between the value of the asset and the liability. The likelihood of losses in respect of these matters is considered to be remote.

Debt

Transpower has given a negative pledge covenant to certain debt holders that, while any debt issued remains outstanding, we will not, subject to certain exceptions, create or permit to exist, any charge or lien over any of our assets.

(ii) Economic gain (loss) account

Transpower operates its revenue-setting methodology within an economic value (EV) framework that analyses economic gains and losses between those attributable to shareholders and those attributable to customers. Under Commerce Commission regulations, Transpower is required to pass onto, or claim from, customers the customer balance at the end of RCP2 (30 June 2020). These balances are spread evenly over the 5 years of RCP3 from 1 April 2020 to 31 March 2025. This results in an NPV equivalent reduction in revenue per annum of $18 million for each year of RCP3.

	HVAC $M	HVDC $M	TOTAL $M
EV balance to be recovered (paid) 1 April 2020 to 31 March 2025	(77.5)	(2.0)	(79.5)

(iii) Environmental hazards

Transpower has a programme of identifying, mitigating and removing environmental hazards such as asbestos at its sites. The cost of mitigating and/or removing identified hazards will vary, depending on the particular circumstances at the site. Where a reasonable estimate of the cost of mitigating or removal of a hazard can be made, a provision has been established.

(iv) Various other lawsuits, claims and investigations

Various other lawsuits, claims and investigations have been brought or are pending against the Group. The directors of Transpower cannot reasonably estimate the adverse effect (if any) on the Group if any of the foregoing claims are ultimately resolved against the Group's interests.

12. Net tangible assets per share

	GROUP		
	2019 UNAUDITED 31 DECEMBER $M	**2018** UNAUDITED 31 DECEMBER $M	**2019** AUDITED 30 JUNE $M
Net assets (equity)	1,690.5	1,588.0	1,640.5
Less intangibles	(373.5)	(369.8)	(372.9)
Total net tangible assets	1,317.0	1,218.2	1,267.6
Net tangible assets per share ($)	1.10	1.02	1.06

The non-GAAP measure above is disclosed to comply with NZX Debt market listing rule 2.3 (f).

13. Subsequent events

On 28 February 2020, the board of directors approved the payment of an interim dividend of $66.0 million to be paid on 20 March 2020. The dividend will be fully imputed.

In addition, on 28 February 2020, Transpower announced it is considering an offer of unsecured, unsubordinated fixed-rate bonds to New Zealand retail investors and to institutional investors.

The directors are not aware of any other matter or circumstance since 31 December 2019 that has significantly, or may significantly, affect the operations or financial statements of Transpower or the Group.

TRANSPOWER