

# Responding to changes and challenges

“Around the world the energy market is changing and the year just past has indeed been challenging. Market structures are evolving as legislative and regulatory reforms complete the move to a competitive energy environment and Australia is no exception.”

Over the coming years every home and business in Australia will have the opportunity to choose their supplier, not just for their gas and electricity, but all other utility services as well.

In this environment AGL is entering one of the more important periods in its long history. With a great track record as a utility, we have embarked on the transition to become a winning energy company. Our future growth is dependent on ensuring we are market leaders with sustainable competitive advantage in all our business activities in order to deliver long-term value creation for our Proprietors.

**“Our future growth is dependent on ensuring we are market leaders.”**

Strategically, AGL plans to build its future on investing in energy infrastructure, managing energy infrastructure and marketing energy products and services. We will continue to develop businesses in those sectors, with the intention of providing a better balance of returns from the regulated and non-regulated sectors.



Greg Martin  
Managing Director

### The New Zealand situation

To a significant extent the smooth implementation of our strategy was disrupted by the events in New Zealand. Since year end our 66%-owned subsidiary Natural Gas Corporation Holdings (NGC) has eliminated from its portfolio the considerable risks faced in retailing electricity in a highly-volatile marketplace.

As a consequence of the actions taken to address the situation, NGC can now rebuild its business on a smaller, but much more stable, platform.

**"AGL's other major businesses have performed well and the underlying strength of the Company is intact."**

While things have not gone as well in New Zealand, AGL's other major businesses have performed well and the underlying strength of the Company is intact. With an experienced leadership team and a skilled and motivated group of over three

thousand colleagues, AGL is well placed to thrive in the increasingly competitive energy market.

### Energy Sales & Marketing

Building on our strategy of dual fuel retailing, we've increased our market presence in south-eastern Australia to a position of market leadership. At year end the AGL Group had almost two million customers buying either natural gas or electricity or both, making us the largest energy retailer in the country both by customer numbers and by units of energy sold. As consumers around the country are given the choice of energy retailer, AGL is well placed to offer both fuels as well as other services to an even wider range of Australian homes and businesses.

Over the next few years Australia will see the completion of the introduction of a fully-competitive energy market. The open marketplace will mean every business and every household will be able to purchase their gas and electricity from the supplier of their choice. To date we have seen the gradual introduction of competition for

industrial and commercial customers for both gas and electricity in most states. I'm pleased to report that the Company has flourished in growing its business in those markets.

**"We've increased our market presence in south-eastern Australia to a position of market leadership."**

We are confident that we will not see a duplication of the New Zealand electricity supply and demand situation occurring in Australia. Here there is a viable hedge market. There are many more generators and many more retailers. In fact, there are 73 registered code participants. The market is well supplied with coal and natural gas and is not dependent on the vagaries of the weather.

The principal issue facing Australian electricity retailers is the potential shortage of peak demand capacity for the few days of summer temperature extremes.



Les Fisk  
Group General Manager  
Corporate Services &  
Company Secretary



John Fletcher  
Group General Manager  
Finance



Michael Fraser  
Group General Manager  
Energy Sales & Marketing



Ian Woodward  
Group General Manager  
Corporate Development

## The management committee

To address this risk in South Australia and Victoria, we decided that the best way to ensure availability of necessary electricity volumes and a level of price certainty during peak demand times was to control our own peaking electricity generation capacity. This additional commitment to power generation highlights the close relationship between producing power and selling it to the end-consumer.

**"This additional commitment to power generation highlights the close relationship between producing power and selling it to the end-consumer."**

We are enhancing our competitive position and lifting reliability of supply to our customers by installing up to 400 MW of gas-fired peak generation capacity with new power facilities in South Australia and Victoria. Construction of these plants is now well advanced, with the majority of this capacity expected to be in operation early in the 2002 calendar year.

#### **Agility**

Only recently created as a manager of energy infrastructure, our infrastructure management and services business Agility has demonstrated its ability to contribute to AGL's bottom-line profit by delivering project benefits to asset owners within a very competitive market. A major infrastructure expense for asset owners is the operation and maintenance of their assets.

Increasingly, we believe both utility infrastructure owners and Regulators will recognise the wisdom of employing specialist organisations as the most cost efficient means of providing management, operations and maintenance services to extract the best returns from their assets and best results for their customers. Our newly created business Agility has been structured to serve those markets. We are proceeding with caution in this direction and we believe the third party market will develop, but we need to be cognisant of our investment returns and efficiencies at the core level.

#### **ActewAGL**

In the Australian Capital Territory through the joint venture between AGL and the Actew Corporation, a new venture, ActewAGL commenced trading in October 2000 and is now servicing the needs of over 136,000 customers in the ACT and adjoining areas of NSW.

ActewAGL has given us the first opportunity in Australia to demonstrate the benefits of the multi-utility model. Customers in the ACT are now billed by ActewAGL for their natural gas, electricity, water and sewerage services. In a short period of time, it is proving to be an excellent example of the way in which multi-utility services can be provided to customers through one organisation. The early returns to AGL from this business are also very encouraging.

#### **New Directions**

Exploring new opportunities during the year we acquired telecommunications and internet services retailer Dingo Blue and,

adding to our previous infrastructure investment in VDSL fibre-optic business TransACT, we agreed to a 20% investment in COMindico, an internet protocol based wholesale telecommunications network.

At first glance AGL's foray into telecommunications appears a world away from our traditional energy base. A closer look, however, reveals a logical progression and a modern adaptation of our skills and expertise to develop additional products and services for our customers and extend our infrastructure portfolio.

Dingo Blue is still in its formative stages and is at present not profitable. In addition to the original purchase price of \$21 million a further \$34.2 million has been provided to fund operating cash flow and working capital requirements. While significant progress has been made in integrating this business within AGL's sales and marketing operations, the decision was taken to write down the carrying cost of the business to \$33 million.

#### **Planning for future growth**

AGL remains in an excellent position to build on the strengths of our key businesses and plans to become a winning energy company at every level. A detailed analysis and review of the whole business has been commenced and is at present in progress.

**"The planned introduction of a fully competitive energy market is still in progress."**

While our strategic direction remains unchanged, execution of the strategy is also being comprehensively reviewed at this time.

The planned outcome of this process is significant improvements in efficiency across all of our businesses and the creation of a solid foundation for building the capabilities required to take full advantage of the many opportunities which will inevitably flow from the continually changing and dynamic energy market.

Included in the review is an examination of the structure of the balance sheet, the management of capital, achieving the right balance between risk and reward and an assessment of the role and longer term value of each business in the portfolio. We will seek out new profit opportunities and review the place of our non-core investments.

We are bearing in mind a number of key guiding principles as we transform ourselves into a winning energy company, all of which we think are important as we develop our re-focused, more executionally-based strategy model:

- enhancing capabilities in our existing businesses;
- creating positions of market leadership;
- developing superior value propositions for our customers;
- optimising capital structures for the assets in our portfolio; and
- sharing the skills of our people across the energy value chain.

To deliver on these drivers, we will operate all of our business operations to 'best-in-class' standards. Our business strategies are built on creating and maintaining competitive advantage in all of the markets in which we participate.

The coming year will see us focused in our efforts to build on our strengths as a major retailer of gas and electricity and associated products and services and as a major investor, manager and developer of infrastructure assets and energy businesses.

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I would like to take this opportunity to thank all my colleagues, who together are AGL, for their willingness to grasp the challenges of a constantly evolving organisation and industry. A special thank you also to the many thousands of loyal AGL Proprietors for their continued support. I have every confidence that over the coming years this loyalty will be well rewarded.



G J W Martin, Managing Director, 23 August 2001

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