

I am pleased to report to Proprietors our resolve to move forward with a clear strategy for the future, building on the Group's core strengths in the downstream energy sector.

Our strategy on how best to grow AGL profitably for the benefit of our customers, our staff and our Proprietors was refocused as we reflected on the difficulties of our New Zealand subsidiary and the strategic rationale behind our investment in telecommunications.

We began the process with a close examination of our position in the market. We were the largest energy retailer in the Australian marketplace. We had a solid business made up of a number of different parts of the downstream energy chain: regulated infrastructure businesses; a business that managed and serviced energy transportation assets and developed new energy projects; and a national sales and marketing business with footprints in NSW, the Australian Capital Territory, Victoria and South Australia.

Our concentration, we decided, would continue to be on developing our position of market leadership in the downstream energy sector because that was where our experience, history and the skills and capabilities of our people lay. At the same time, we needed to develop a sustainable business model that, while cognisant of the nature and size of the Australian marketplace and our position in it, could fully exploit our core businesses and competencies to maximise Proprietors' returns.

Given this framework, we set about developing a strategy for our future. The strategy was built around four parts: filling the gaps identified in our business platform; building on our strengths and extracting full value from our existing businesses; reconfiguring our portfolio; and continuing to develop our Company culture and capabilities into an unbeatable competitive asset.

The first part of the strategy is not simply a matter of filling the gaps we identified in our business platform. While it had been clear to us for some time that a major gap for AGL was gas retailing in Victoria, the strategy was driven as much by the need to have a better balance in our business. We needed balance in earnings from both regulated and market-based businesses. We needed balance in the nature of those earnings, that is earnings with both yield characteristics and capital growth. We also needed to balance risks appropriately, given that the risk profile of our business was changing.

As the Chairman has noted in his Report, the acquisition of Pulse Energy, in July this year was an important

acquisition for AGL. It represents a compelling and strategically important acquisition for the Company as it fills several gaps in our energy sales and marketing activities in the Victorian market – the second largest in the country. Indeed, I do not believe there was another energy company better positioned to extract as much value from the acquisition as we can.

Of course, no matter how exciting an acquisition is, the proof of the pudding, always, is in how well the new business is integrated. I can assure Proprietors that every effort is being expended to ensure our experience from past successful integrations of new businesses into AGL is applied to Pulse Energy. The leaders of the work teams involved in the Pulse Energy integration are the best in our business and I have every confidence that the acquisition will live up to its promise by delivering tangible returns to Proprietors.

Our long-term Proprietors will recognise our track record in this area. The acquisition of Solaris Power in Victoria and ETSA Power in South Australia moved AGL from a single-state gas company to a multi-state downstream energy company. Pulse Energy again moves AGL to a position of leadership as the largest downstream energy company in Australasia.

The integration process links back to the second part of our strategy, which is extracting full value from our existing businesses. AGL continues to benefit from businesses that provide solid organic growth opportunities. During the year we continued to grow our energy networks with new connections to both electricity and gas networks.

Our Agility business continues to blossom and is establishing a reputation as the country's leading designer, constructor, manager and operator of downstream energy infrastructure. It has completed a number of successful projects for clients around the country over the past twelve months and made good progress, both in profitability and in positioning itself for growth.

In New Zealand, there is now much more dialogue and interaction between AGL and our subsidiary there. We are moving to unlock further synergy benefits while at the same time working with NGC to assist it for future growth, earnings and cashflow returns to AGL.

Reconfiguring our portfolio, the third part of our strategy, resulted in a decision to exit from retail telephony products. Our original intent in purchasing Dingo Blue was to add a range of retail telephony products to our



gas and electricity retailing business. Our experience with this business, together with our strategy review, confirmed that the telecommunications sector was not part of AGL's core activities going forward. As a result, all fixed line and internet services offered by Dingo Blue terminated on 31 May 2002. We are currently pursuing a number of claims against Optus that relate to the original purchase and we are working towards the closure of the mobile telephone service.

Likewise, we have earmarked our investment in COMindico as a non-core asset and will be working with the other major shareholders to successfully complete the internet protocol network and the full product range being offered by COMindico. We are encouraged at the take-up rate of products and services already being sold into the market by COMindico and will look to profitably exit from this business at an appropriate time.

Ensuring appropriately flexible energy trading operations underpins decisions on reconfiguring AGL's business, including the acquisition of Pulse Energy. The power generation plants being built in Victoria and South Australia will substantially meet the very high peaks in demand on extreme summer days during the year in those markets. In addition, and very importantly, they will act as an insurance policy by providing greater pricing certainty during periods of extreme demand.

On the subject of competitively priced wholesale energy, work has continued during the year on securing competitively priced gas for our future. Our 30-year contract with the Cooper Basin producers will be coming to an end in the next few years. While the Pulse Energy acquisition has given us access to the principal Victorian gas contract supplied from the Bass Strait gas fields, it has not diminished our recognition of the need to build a competitively priced portfolio of gas contracts from multiple producing basins and parties. This includes potential new northern sources of both natural gas and coal-seam methane gas.

Another significant area of work this year has been in the vitally important area of risk management. We recognise that AGL continues to change, as does the nature of the risks experienced in a competitive marketplace. Nothing illustrated this more clearly than our experience in New Zealand last year. During the year Management, with full Board support and encouragement, completed a very detailed process of identifying how best we manage the major risks in AGL, both in terms of looking at the raw

risks we face and the controls that are in place to manage and mitigate them.

The fourth and final part of our strategy concerns enabling us to make the changes that we need to, both culturally and operationally to ensure the above three parts of the strategy are delivered. We are continuing to develop AGL's high performance culture where an individual's remuneration and rewards are being directly tied to the achievement of the business objectives flowing from the strategy.

We will also continue to focus on building capability and leadership in the business. AGL needs a strong talent bench to deliver our strategy and this can only be achieved by creating a pool of talented people. Our clear goal is to attract, retain and grow talented people in an open and honest culture where individuals feel rewarded and recognised for the contributions they make.

While much is changing in AGL, one thing that remains constant is the commitment to nurture the values that have guided us as an organisation through good times and not so good times. We remain committed to advancing the interests of our Proprietors as we do to promoting the safety and wellbeing of our people and those who contract their services to us. Also high among our priorities is nurturing the associations we have built up in the communities in which we operate, as well as ensuring that our activities do not harm or damage the environments in which we do business.

We look forward to the future with great confidence. AGL's core energy businesses are performing well. We have a clear strategy that is focused on building upon our position of market leadership as well as a continued resolve to improve the performance of AGL.

Greg Martin  
Managing Director

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