M John Phillips AM
Chairman

Chairman's Report

Dear Shareholder,

I am pleased to report that your Company has returned to its path of improving profits and increasing Shareholder returns. That this has occurred despite highly competitive trading conditions and tight regulatory constraints is particularly pleasing and is a credit to the Management and staff.

Profit attributable to Shareholders in 2002/2003 was $295.0 million compared with $192.1 million in 2001/2002 and $115.4 million in 2000/2001. Earnings per share was 67.3 cents, up from 51.6 cents in the previous year.

The Board has approved a final dividend of 29 cents a share, franked to 18 cents. This will be paid to Shareholders on 26 September 2003 and will bring the total dividend for the year to 55 cents (34 cents franked). You will recall that recent changes to the Company's Constitution have meant that the declaration of dividends no longer needs to await the Annual General Meeting, so they may now be paid earlier to Shareholders.

There is a Foreign Dividend Account (FDA) credit of 4 cents attached to the final dividend for the year.

The Dividend Reinvestment Plan will again be available with the discount unchanged at 2.5%.

A year ago, the Board set a number of challenges for the Company to achieve in 2002/2003. Virtually all were met.

The Pulse Energy business, acquired in July 2002, was successfully integrated into AGL and has been providing the expected returns. NGC Holdings Limited, our 66%-owned subsidiary in New Zealand, has restructured its operations, exiting the gas and electricity retailing business and selling its power generating assets. The New Zealand business is now tracking well and a capital return to shareholders from NGC of NZ$525.0 million (AGL share NZ$346.8 million) is planned for later this year.

In December 2002, we negotiated a new 15-year portfolio of wholesale gas supply and transportation arrangements for the NSW, Victoria, Queensland and ACT markets. This is a very important element in our efforts to ensure long-term supply reliability to our gas customers.

Regrettably, the nature of the electricity market, and the regulatory arrangements surrounding it, make it more difficult to secure a similar level of long-run reliability of supply for electricity customers. However, we are doing what we can towards that end also.

As an indication of the strength of the Company's normal operations, profit after tax, but before significant items, was $320.8 million in 2002/2003 compared with $247.1 million in the previous year, an increase of 30%. There were again a number of significant items, which are listed in the Financial Statements. One I would mention is the COMindico adjustment.

The restructuring in the ownership of COMindico, which occurred during the year, coupled with AGL's ability to appoint a Director to their board, has meant that we need to equity account our investment in the company this year for the first time. As a result, AGL has recognised its share of COMindico's losses from the date of its original investment in September 2000 through to June 2003, totalling $52.5 million. This includes the $10.0 million that I told you about when we announced the December 2002 half-year results. The carrying value in AGL's books is now $19.5 million.

The lower carrying value means that, if our current assessment of COMindico's potential is confirmed, its eventual net value (in excess of carrying value) will be that much higher.

Since the end of the financial year, AGL together with its consortium partners, Tokyo Electric Power Company (TEPCO) and financial investors led by the Commonwealth Bank of Australia, have entered into a conditional share sale agreement to purchase Loy Yang A Power Station and its adjacent coal mine in Victoria's Latrobe Valley.

As I write this letter, we are still in negotiations with the Australian Competition and Consumer Commission (ACCC) so I will not seek to canvass in any detail the issues that might be of concern to the Commission. We see the purchase as consistent with our strategy of securing competitive investment opportunities in power generation, and complementary to our approach of spreading investments across a variety of energy assets.

AGL would hold a 35% interest in Loy Yang Power, as would TEPCO, and structures would be put in place to ensure that it would continue to trade with all electricity retailers, including AGL, on a strict arms-length basis. Our commitment to these structures has been part of our submission to the ACCC from the outset. The purchase is seen by the Board as an important step in supporting supply reliability in that state and in south-eastern Australia more generally.

AGL's strong balance sheet, recognised by the decisions of both major rating agencies to confirm our A credit rating, means that the Loy Yang transaction can be funded from existing credit lines, while still leaving the Company with a very satisfactory debt : debt plus equity ratio.

Corporate Governance has been a topic of much debate following the spate of corporate collapses and the subsequent release of the Australian Stock Exchange's (ASX) Corporate Governance guidelines.

AGL was already conforming with most of the ASX guidelines, as you will see from the Corporate Governance section of this Annual Report. However, it needs to be said that good governance is more about behaviour and relationships, about embedded values, and about the integrity with which boards and management go about their business than it is about ticking boxes and adding further pages to annual reports. AGL strives for high ethical standards in all its dealings, with our customers, our staff, our Shareholders, the regulators and the community. That will continue to be our aim.

That said, we are acutely aware that we do not operate in a vacuum. We are now a large company, in fact the largest in some sections of our industry. Our activities affect the daily lives of a substantial part of the Australian population, and society's expectations of energy companies, as suppliers of an essential national service, are high. On top of this, there has developed a suspicion of 'big business', sometimes understandable, sometimes fostered for various purposes by sections of the political spectrum and the media. These factors have caused us to reflect even more deeply on the way we conduct our business and provide our products and services.

Particularly with the continued growth of our business, and our expansion into Victoria and South Australia, we have been looking closely and critically at what Corporate Social Responsibility means to AGL, and how we might strengthen our community relationships and partnerships, not just to enhance our image or foster business, but to give sharper focus to decisions on the community and charitable activities in which we might engage. We are well down the path to finalising that exercise.

It is sometimes said that the sole task of a board is to maximise profit for its shareholders. That is not AGL's credo. We certainly seek to ensure that our Shareholders are well rewarded for their investment, consistent with the risks involved and comparable with other similar investments. But we would go further than that. In a democracy like Australia, every element of society, whether an individual, a group or a corporate entity, owes responsibilities to every other element and to the community in general. Our aim is to be able to say that we have discharged all those responsibilities.

Events overseas continue to demonstrate how important it is for Australia to have an efficient energy industry, supported by an effective national energy market.

Reforms over the past decade have been positive in this respect but there is still much room for improvement. The need to improve infrastructure in some states has been well demonstrated and we are still well short of a national market. I welcome the final report of the Energy Market Review, known generally as the 'Parer Report' which was sponsored by the Council of Australian Governments, and generally support its recommendations, albeit with some reservations on details.

I have little doubt that a national energy market will come, with a major shift towards real competition. At AGL we have been positioning ourselves for this for more than a decade, moving from a single-state, single-fuel gas company to a national energy company, now with more electricity customers than gas customers, and operating in all states except Tasmania.

How much longer we must wait, I cannot say. I am encouraged by developments now in train to create structures for a national market but there are some tall hurdles still to be cleared. We won't have a truly national market, with all players competing on their merits and on equal terms, until we have a clear and stable policy direction, and a separation of roles between policy makers, regulators and market operators.

We also need greater consistency of regulation across jurisdictions. I said to you last year "the problem is not just the proliferation of regulators. The system is inconsistent between forms of energy; it pays little attention to national energy objectives; it introduces substantial discontinuity between different parts of the market, particularly in the electricity market; and it fails in its stated aim of balancing the objectives of consumer protection, competition and the encouragement of investment."

That is not to downplay the importance of having a national regulator, providing it is a regulator dedicated to and skilled in the intricacies of the energy market, not just a department of a mega-regulator like the ACCC. The recent success of mega-regulators in avoiding major disasters, not just in the energy sector, has not been impressive.

Subject to there being even-handed and fair regulation, the future for AGL looks bright. We believe there is scope for expansion both through acquisition and through organic growth in our existing portfolio. In the coming year, we will be focusing on fundamental improvements in our operations with the object of retaining existing customers and attracting new ones without damaging overall profitability.

To achieve that, we will be relying on the dedication and commitment of our AGL staff. We are fortunate in the calibre of the people employed in all sections of the Company. They have again performed magnificently in a very challenging and busy year. On your behalf, and on behalf of the Board, I thank them for their loyalty and their hard work. To that I would add my thanks to the Managing Director and his Management team for their efforts in getting the Company back to a successful path, and to my fellow Board members for their commitment and their support.

M John Phillips AM
Chairman

21 August 2003