The Treasury

Solid Energy Information Release

March 2013

Release Document

www.treasury.govt.nz/publications/information-releases/solidenergy

Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[2] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information, or who is the subject of the information

[3] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[4] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[5] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice

[6] 9(2)(j) - to protect the commercial position of the person who supplied the information, or who is the subject of the information; to enable the Crown to carry out commercial activities without disadvantage or prejudice; and to enable the Crown to negotiate without disadvantage or prejudice

[7] 9(2)(ba)(i) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely to prejudice the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied

[8] Information is out of scope or not relevant.

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, a [3] appearing where information has been withheld in a release document refers to section 9(2)(f)(iv).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

ccmau CROWN COMPANY MONITORING ADVISORY UNIT
TE MATA AROTURUKI RAWA A TE KARAUNA
Protecting and enhancing shareholder value

Solid Energy: Briefing for Meeting with Chair (John Palmer) and CEO (Don Elder) on Thursday 20 March 2008

To	Minister for State Owned Enterprises	**Priority**	Urgent
Date	19 March 2008	**Deadline**	20 March 2008

Purpose

You are scheduled to meet with the Chair, John Palmer, and CEO, Don Elder, of Solid Energy on Thursday 20 March 2008 between 11.45am and 12.15pm. The meeting follows Solid Energy's Commerce Select Committee meeting.

It is a chance to discuss Solid Energy's disappointing financial performance for the six months to December 2007, limited acceptance of the land disposal process, new energy developments, and other issues facing Solid Energy.

Company background

Solid Energy's core business is the mining of coking coal for export markets and thermal coal for Genesis' Huntly power station, NZ Steel and a number of industrial customers. Solid Energy is also investing in alternative energy forms such as coal-to-gas options, development of the Southland lignite resources, pellet fuels and bio-fuel.

For the 2006/07 year, Solid Energy's net profit after tax (NPAT) of $94.1 million on revenue of $564 million, represented a return on equity of 33.6%. The result included a $55 million one-off gain from the sale of a 49% stake in the Spring Creek mine. For 2006/07 NPAT was forecast at $21 million on revenue of $482 million.

Financial performance for the six months to 31 December 2007

Solid Energy reported a disappointing net loss after tax for the half year of $2.7 million against a budgeted NPAT of $12.0 million. Coal sales volume fell 16% from the prior year to 1.95 million tonnes; 11% below budget. Revenue was also 11% below budget.

The loss was due to several factors including:

- reduced volume from the Stockton mine due to reworked production schedules, wet weather, rail line closures and strike action
- increased Stockton production costs of $81/tonne versus budget of $60/tonne
- Huntly sales to Genesis and NZ Steel not meeting budget

Further detail on the financial performance compared to budget is in Annex 1.

The Stockton mine is expected to reach planned levels in the second half of the year, with Spring Creek commencing full production in January 2008, leading to a strong second half year. NPAT is now forecast at $19 million, compared to the plan budget of $21 million.

Limited acceptance of the Land Disposal Process

Solid Energy has advised it is reluctant to commit to the permanent land disposal process for land it has acquired under normal commercial terms (this does not include land acquired by Solid Energy under the Asset Transfer Agreement 1988).

On 23 January 2008, you sought an assurance from Solid Energy that it would do all it could to meet the government's process for land disposals, and that it would maintain its commitment to the no surprises policy. Solid Energy agreed to advise CCMAU before entering into binding contracts, but you may wish to advise the Chair that your expectation is that sufficient notice will be provided to CCMAU to allow alternative options to be considered should shareholding Ministers prefer that a sale not proceed.

New Energy Developments and the NZ Energy Strategy

Solid Energy continues to develop plans for the use of Coal Bed Methane gas in the Waikato and the Southland Lignite deposits (as detailed in their 2007/08 strategic plan) and has spoken about these proposals at recent energy and petroleum conferences. Although at differing stages of development, the use of such thermal resources may be restricted by the ban on new thermal generation capacity.

Solid Energy supports debate on the NZ Energy Strategy which holds many challenges for a mining company. This includes the impact to its own business activities (such as higher fuel and electricity costs), but more importantly on its major customers such as Genesis and NZ Steel. While Solid Energy accepts the need for New Zealand to move toward cleaner sustainable forms of energy, it believes this should not be done at the unnecessary expense of the country's growth and prosperity.

Other issues

Board Appointments

John Spencer, Deputy Chair, completes his first board term in April 2008 and you have indicated he will be reappointed. West Coast-based Tony Williams completes 6.5 years in April 2008, and you have indicated he will be replaced by Simon Marsters.

Switch Energy Opening

Switch, Solid Energy's new renewable energy brand, has opened its first showroom in Christchurch. It will design and supply integrated heating systems using solar hot water heating, central heating boilers running on wood pellets, specialist hot water cylinders and control systems which ensure connected systems operate as efficiently as possible.

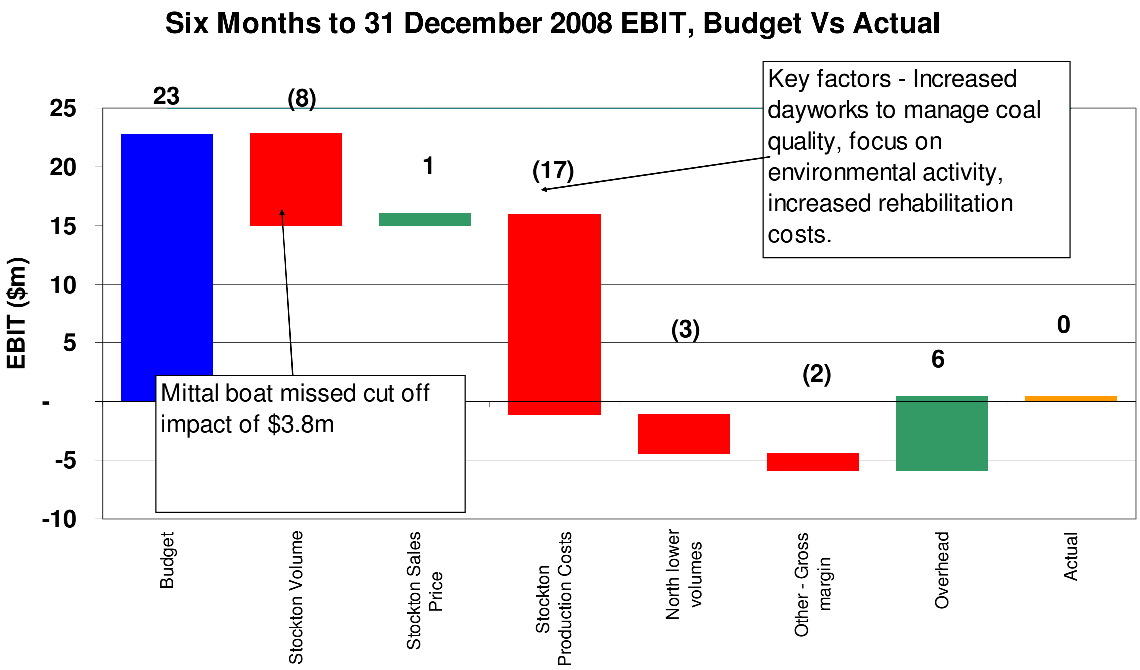
Michael Moore
Manager – Energy, Land & Environment
CCMAU [1]

Hon Trevor Mallard
Minister for State Owned Enterprises

Annex 1. Financial performance for the six months to 31 December 2007

The following commentary is provided as background on Solid Energy's disappointing financial result for the six months to 31 December 2007.

Solid Energy's waterfall chart below shows the key variances between budgeted earnings before interest and tax (EBIT) of $23 million and the actual of -$0.5 million.



Stockton Volume ($8 million negative variance)

Delays in accessing the ridgeline mining area and the associated need to rework production schedules, a prolonged period of wet weather, Midland rail line closures, strike action and increased quantities of by-product coal have all contributed to production at Stockton being 157 kilo-tonne (kt) down on budget. Total sales of 843kt were 128kt behind forecast which, based on the budgeted margin of $62/tonne, gives rise to a negative variance of $8 million.

The export business typically has a relatively small number of high value sales transactions. The late arrival of a 62kt export ship, which sailed just after the half year close, alone accounted for a variance of $3.8 million on budget.

Stockton production costs ($17 million negative variance)

Over and above the reduction in volumes, costs on a per tonne basis increased from a budget of $60/tonne to an actual of $81/tonne.

Approximately $15 million of these overruns is due to several unbudgeted factors which have reduced production at Stockton. It is difficult to quantify the individual impact of these items, but they included:

- increased dayworks from unplanned pit mix changes to manage coal quality in order to meet sales orders (part of the continued impact of short-term compromises made to the mine plan during the previous 12-24 months due to ridgeline mining and snail management issues

- a deliberate focus on environmental projects to progress the Stockton Water Management project, and improve day to day water management performance
- poor weather including rainfall and fog
- some impact from rail disruption
- rehabilitation amortisation costs increased by $2 million over budget due to changes to the discount rate applied to future expenditure, which is now based on Government stock, and is consistent with NZ IFRS.

Huntly North Volume ($3 million negative variance)

Sales to Genesis were down on forecast by 64kt as a warm winter and increased gas usage reduced demand for coal. Sales to NZ Steel were down by 46kt due to [2]

Overhead - resource proving and R&D ($6 million positive variance)

There have been some timing delays in resource proving in the coal business ($3 million favorable) and timing delays in New Energy feasibility study spend, however all major initiatives are considered on track.

Full year forecast

Solid Energy is forecasting strong second half performance and now forecasts an NPAT of $19 million for the 2007/08 financial year; a recovery close to budget of $21 million. Slippage of a June export shipment into July could reduce the actual result however.

Spring Creek and Stockton volumes are forecast much higher in the second half year:

Mine	Jul-Dec 07	Jan-Jun 08	Total 07/08	Forecast 08/09
Stockton Mine	843	1,036	1,879	1,491
Spring Creek Mine*		275	275	700
Total	843	1,311	2,154	2,191

** Solid Energy owns 51% of Spring Creek mine which began production in January 2008.*

While there has been a significant leap in spot international coal prices, this will not flow into benchmark contract prices until the next financial year. Stockton volumes are expected to be lower in 2008/09 due to a continued focus on optimising the long term mine value/mine plan and progressing environmental objectives such as completing the Stockton Water Management project.