

Proposed Strategic Alliance between Air NZ and Qantas



MATERIALS FOR DISCUSSION

CONFIDENTIAL | DECEMBER 2002

Introduction

First NZ Capital was appointed in July 2002 to evaluate the proposed Strategic Alliance Agreement (SAA) from the perspective of the Crown as the major shareholder in Air NZ

Initially our evaluation involved a qualitative assessment of the commercial terms being considered by Qantas and Air NZ

By mid November, the commercial terms were substantially improved for Air NZ and largely agreed between Air NZ and Qantas

At this time we were provided with financial projections for Air NZ

- with the proposed Joint Airline Operation (JAO case) and
- without the proposed JAO (stand-alone case)

Financial projections were prepared for three competitive scenarios for each of the JAO and stand-alone cases

During the process we held discussions with Air NZ management and its legal and financial advisors on numerous commercial and financial aspects of the proposal

Key Conclusions

SAA Positive For Air NZ

SAA should provide substantial benefits to Air NZ
Improved financial performance, stronger financial position and higher underlying value
Future viability as an international airline substantially enhanced

SAA Value Enhancing for Crown

Higher Air NZ earnings increases underlying value of the Crown's shareholding
Improved operating balance for Crown (higher earnings and reduced debt to consolidate)
Potential requirement to inject new equity significantly reduced

Governance Largely Unaffected

Crown's rights as majority shareholder largely unaffected – would continue to elect majority of Air NZ board
Qantas shares in management of Air NZ through SAAG
Crown's scope to sell shares restricted to Qantas and/or placement to retail and/or institutional investors

The proposal should be value enhancing for the Crown, and reduce the likelihood of the Crown being required to contribute new capital to Air NZ.

Governance and Management

Constitution

Proposed constitutional changes not material

- written resolution to be signed by Qantas director
- Qantas director required for quorum at board meetings
- if no quorum, Air NZ chairman can adjourn for 24 hours and hold meeting without Qantas director

Qantas provided anti-dilution rights to maintain 22.5% shareholding

Board Representation

Qantas has right to nominate two board representatives

Crown can vote on nominations as it desires

- if votes against Qantas nominees Qantas can terminate SAA

Through majority shareholding (63.5%) Crown maintains right to elect board

Air NZ Management

Qantas would have substantial management influence through SAAG

JAO governance principles do not restrict Air NZ board's rights and obligations

Financial Impact of SAA on Air NZ



Financial Implications for the Crown

Limited scope to sell any shareholding to potential strategic partners, except Qantas, without

- Qantas' consent or providing Qantas with the right to terminate SAA

currently no serious strategic partners, other than Qantas

Crown can place shares to institutional and retail investors

if SAA is not implemented, in our view, the Crown would be required to inject additional capital to maintain Air NZ's international network

Other Material Matters

Strategic alternatives to JAO

- partnership with Virgin Blue offers limited benefit
- limited interest from other potential investors
- no other airline can offer same benefits to Air NZ

Capital raising