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**To:**  
Dr Michael Cullen

**From**  
Rob Cameron

**By**  
Facsimile

**Date**  
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## **Air New Zealand Update**

This note provides an update on Air New Zealand. The week ahead is shaping up to be critical. It will provide a clearer picture as to the viability of the proposed recapitalisation plan and of the extent of the Crown's capital participation.

Work between Air NZ and Singapore Airlines is continuing towards identifying the immediate capital requirements for the recapitalisation plan. The key issues for this week are:

- Whether Air NZ and Sir Richard Branson reach a final agreement (conditional only on ACCC approval) for the sale and purchase of Virgin Blue;
- Advice of the final immediate recapitalisation requirements; and
- Extent of Crown and other shareholder support required for the recapitalisation.

If the negotiations with Sir Richard Branson are successful, the Crown will be asked to provide a letter to Air NZ's auditors indicating its support in principle for the recapitalisation to enable the accounts to be certified with Ansett valued as a going concern. This avoids a material write down that would lead to Air NZ breaching its banking covenants.

### **Media Statement**

The next step would be for the Government to make a preliminary announcement to the media indicating that it had negotiated a package of measures with Singapore Airlines to accommodate the recapitalisation as outlined in the Cabinet paper. This statement would be accompanied by a statement from Air NZ outlining the status of the recapitalisation plan.

We would like to work with your office to develop the Government's media statement. Before release, both the Government and Air NZ statements will need to be agreed by the Government, Air NZ and Singapore Airlines.

### Finalising Negotiations with Singapore Airlines

In light of the significant change to Air NZ's situation and the size of the recapitalisation, Singapore Airlines has proposed that the voting rights to shares in excess of 40% are frozen for a period of three years subject to performance against the National Interest Package.

Singapore Airlines also agrees with a reduction in the size of the Air NZ board from 13 to 11 and have requested that governance arrangements require a two third majority approval for a number of matters including changes to authorised capital, appointment and removal of the Chairperson and Chief Executive, major transactions and financial policy. Our preliminary view is that these proposed measures are reasonable. In any event, these measures involve changes to the Constitution that will require approval of 75% of each class of existing shareholders.

We expect to finalise negotiations with Singapore Airlines and Air NZ relating to governance, the national interest package and changes to the Constitution this week.

An outstanding issue to be discussed with Singapore Airlines is the appointment of the Chairperson of the Board.

### **Brierley Investments**

We are also discussing with BIL their future role in the financing and governance of Air NZ. Their position is unclear but should be resolved at a Board meeting today.

### Alternative Scenario

If Air NZ and Sir Richard Branson are unable to reach agreement on the Virgin Blue acquisition, the Air NZ directors will immediately have concerns about finalising the accounts without breaching the banking covenants.

It is likely that the directors will want to inform the market of the state of play before the end of the week.

Air NZ and Singapore Airlines are developing options in the event that negotiations are unsuccessful. In broad terms these involve a distressed sale of Ansett to the Australian government and/or Qantas. In these circumstances, Air NZ is unlikely to avoid a breach of its banking covenants and may face insolvency.

At some stage Air NZ will undoubtedly seek financing from the Crown. In the absence of a sale of Ansett, it is not clear that anything other than a very large amount (eg \$1.5-2 billion) would satisfy the directors regarding their ability to keep trading. If Ansett is sold, then the capital sought from the Crown may be lower.

Air NZ is likely to seek the assistance of the New Zealand government to present its case to the Australian government.

If you wish to discuss any of the above please ring Rob Cameron on                      or Murdo Beattie on                      .