

The Treasury

Strategic Issues and Shareholder Expectations Letters Information Release

Release Document

April 2015

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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)(ba)(ii) - 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 otherwise to damage the public interest
- [4] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
- [5] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [6] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [7] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice

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 [1] appearing where information has been withheld in a release document refers to section 9(2)(a).

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

5 March 2015

The Hon Todd McLay
Minister for State Owned Enterprises
Parliament Buildings
WELLINGTON

The Hon Bill English
Minister of Finance
Parliament Buildings
WELLINGTON

The Hon Steven Joyce
Associate Minister of Finance
Parliament Buildings
WELLINGTON

Dear Ministers

STRATEGIC ISSUES FOR 2015/16 – 2017/18 BUSINESS PLAN

Thank you for your letter of 19 December setting out the Shareholder's Expectations for 2015/16. The Board confirms that Airways strategy will deliver outcomes aligned with Shareholder Expectations.

The Board has provided a brief response to each of your expectations below. The Board has also commented on specific actions Airways is taking to enhance the safety of New Zealand airspace in light of the recent Malaysian airline tragedies and the global security situation.

Entity Specific Expectations

Safety: Airways absolute priority is to deliver a safe and reliable Air Traffic Management system in New Zealand's controlled airspace to ensure that all aircraft and passengers reach their destination safely, efficiently and at reasonable cost.

In the year ending 30 June 2014, Airways controlled over one million aircraft movements and had zero high severity safety incidents involving scheduled airline aircraft. Based on CANSO data, this places Airways amongst the top 10 safest Air Traffic Control providers in the world. Internally, Airways has a strong staff safety record and had zero serious injuries amongst staff in the year ending 30 June 2014. The Board and management are totally committed to maintaining this very high level of safety performance. The Business Plan will include significant initiatives to continue enhancing Airways Safety Management System as the prime strategy to drive proactive safety improvement, improve productivity and increase customer value propositions.

In the year ending 30 June 2014, Airways achieved a system reliability level of 99.95%, in line with the expectations of aviation customers. Airways will be making significant investments in its Tower assets,

communications networks, navigation aids and contingency centres over the coming year to maintain a high level of service reliability.

Execution Risk related to MANA Strategy: Airways embarked on a transformational strategy in 2012. The strategy was termed Project Mana (“Making a new Airways”). The 10 year strategic goals defined by Mana were to double revenue, triple the value of Airways and create 200+ high quality jobs by 2020 (Airways “2-3-200” goals).

During the first three years of the transformation, Airways has enhanced customer focus, optimised the System Operator business and created three new businesses in Airways Global Services. As a result, Airways is on track to have grown revenue by 13%, increased its valuation by 35% and created 52 new jobs by 30 June 2015. Airways is continuing to progress its transformation. The current business plan is being constructed under the themes of “safe, successful and sustainable”. “Safe” is about maintaining and building on the demanding stretch targets within the System Operator business, “successful” concerns maximising the return from the three new business created under Airways Global Systems and “sustainable” is tasked with protecting the shareholders’ value as the industry undergoes the major shift from radar to satellite based navigation. Airways will continue to keep Treasury up-to-date on its progress, plans and risk mitigation strategies.

Dividends: The Board acknowledges the Shareholder’s note that Airways has been paying a lower dividend whilst it executes its Mana strategy. Specifically, Airways continues to balance the essential capital expenditure programme required to enable the transition to satellite based navigation with the expectation of paying a dividend. Airways confirms that it is on track to continue to raise its dividend in line with the expectations previously agreed with the shareholder. Accordingly, the Business Plan forecasts dividends of \$4m for 14/15 rising to \$5m in 15/16. These are higher than the guidelines set out in Airways dividend policy and reflect Airways commitment to meeting the shareholders expectations.

Generic Expectations

Capital Allocation: Airways notes the expectation of engaging with Ministers and officials on Airways strategic initiatives as they develop, particularly those that involve a meaningful allocation of capital. Airways’ Investment Management Framework requires robust business cases which evaluate options thoroughly, are based on reasonable assumptions, take into consideration all risks and apply the appropriate risk-adjusted cost of capital to ensure the investments are value enhancing. Airways will continue to work proactively with its Treasury relationship managers, Amanda Smith and Jason Yuschik, to keep them fully informed of Airways strategy and up and coming investment decisions.

Strategic Reviews: Airways notes the programme of strategic reviews being initiated by Treasury and the expectation that Airways first review will occur in 2015/16. Airways look forward to working with the Shareholder and officials to maximise the value of the strategic review process.

Non-Crown debt assurance: Airways ensures lenders are specifically made aware that borrowing by Airways does not represent Crown debt and is not accordingly guaranteed by the Crown. Airways confirms that the current facility documentation includes a non-Crown debt assurance clause.

Capital Injections: Airways commercial businesses are self-funding. Airways is not expecting to request any capital injections and notes the high threshold for the Crown to approve any new cash injections.

Early notification of any material change in SCI forecast: Airways maintains a rolling range of expected full year SCI forecast outcomes. The forecast range is included in the quarterly reports to the Shareholder. Airways also informs Treasury of any material changes to the forecast on a timely basis.

Update on Post-Investment Reviews: Airways Investment Management Framework requires post-implementation Benefit Realisation Reviews (BRRs) to be completed for all projects >\$1m. Airways will continue to provide the Shareholder with an annual summary of all post-investment reviews over the defined threshold and make copies of the full reviews available also.

Independent Valuations: The preparation and use of independent company valuations continues to be a key component of Airways business planning process and will be covered in Airways SCI.

Airways Response to the Global Security Situation

Surveillance & Safety: Airways operates a comprehensive surveillance service across the major air routes in New Zealand. The surveillance systems can track all commercial aircraft on the major air routes, including situations where a transponder is not working around the main Airports. Airways is currently implementing new, multilateration technology which extends surveillance coverage to remote areas outside the major air routes and will provide coverage down to very low levels for virtually all of New Zealand and its territorial waters by 2018. Airways is an active member of the CANSO Aircraft Tracking Task Force working closely with ICAO to develop a global standard.

Airways is also actively engaged with MFAT, the World Bank and the Pacific Island nations to promote a comprehensive Pacific Strategy. The strategy would see Airways sharing its capabilities more extensively, working in collaboration with Pacific Island states to share expertise to provide safer and far more robust services across the Pacific Island area.

Security: Airways undertakes quarterly Crisis Management Exercises on multiple scenarios , including hypothetical challenges to physical and cyber security. As experience broadens, Airways has the opportunity to involve customers, related partners and government agencies. All such exercises help further refine the Airways Crisis management Plan and an ongoing comprehensive review of the security of all assets and systems.

The Board and management look forward to working with the shareholding Ministers and Treasury officials to make 2015/16 a highly successful year for Airways, customers and shareholders.

Yours sincerely



Susan Paterson ONZM
Chair