Aurizon Network Pty Ltd

ABN 78 132 181 116

Interim Financial Report for the six months ended 31 December 2018

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Aurizon Network Pty Ltd is a company limited by shares, incorporated and domiciled in Australia. Its registered office and principal place of business is:

Level 8
900 Ann Street
FORTITUDE VALLEY QLD 4006

	Notes	31 December 2018 $m	31 December 2017 $m
Revenue from continuing operations	1	**557.4**	607.6
Employee benefits expense		**(73.5)**	(65.9)
Energy and fuel		**(52.2)**	(76.1)
Consumables		**(75.1)**	(67.3)
Depreciation and amortisation		**(151.1)**	(144.4)
Other expenses		**(6.0)**	(5.4)
Operating profit		**199.5**	248.5
Finance income		**0.1**	0.2
Finance expenses		**(78.6)**	(74.3)
Net finance costs		**(78.5)**	(74.1)
Profit before income tax		**121.0**	174.4
Income tax expense		**(36.7)**	(52.7)
Profit after tax for the six months		**84.3**	121.7

The above consolidated income statement should be read in conjunction with the accompanying notes.

	31 December 2018 $m	31 December 2017 $m
Profit after tax for the six months	**84.3**	121.7
Other comprehensive income		
Items that may be reclassified to profit or loss		
Changes in the fair value of cash flow hedges	**(5.1)**	5.8
Income tax relating to these items	**1.5**	(1.7)
Other comprehensive income for the six months, net of tax	**(3.6)**	4.1
Total comprehensive income for the six months	**80.7**	125.8

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

	Notes	31 December 2018 $m	30 June 2018 $m
ASSETS			
Current assets			
Cash and cash equivalents		**1.4**	2.2
Trade and other receivables		**146.7**	225.2
Inventories		**35.2**	29.9
Derivative financial instruments		**-**	0.6
Other assets		**5.7**	1.3
Total current assets		**189.0**	259.2
Non-current assets			
Inventories		**9.0**	6.7
Derivative financial instruments		**148.3**	108.8
Property, plant and equipment		**5,366.9**	5,407.8
Intangible assets		**97.9**	95.1
Total non-current assets		**5,622.1**	5,618.4
Total assets		**5,811.1**	5,877.6
LIABILITIES			
Current liabilities			
Trade and other payables		**136.4**	115.5
Borrowings	3	**94.0**	51.0
Provisions		**52.7**	54.6
Other liabilities		**32.6**	49.5
Total current liabilities		**315.7**	270.6
Non-current liabilities			
Borrowings	3	**3,299.2**	3,302.5
Derivative financial instruments		**4.5**	21.3
Deferred tax liabilities		**653.4**	637.1
Provisions		**3.4**	4.1
Other liabilities		**174.0**	183.0
Total non-current liabilities		**4,134.5**	4,148.0
Total liabilities		**4,450.2**	4,418.6
Net assets		**1,360.9**	1,459.0
EQUITY			
Contributed equity		**3.7**	3.6
Convertibles notes		**1,200.0**	1,200.0
Reserves		**(16.8)**	(13.2)
Retained earnings		**174.0**	268.6
Total equity		**1,360.9**	1,459.0

The above consolidated balance sheet should be read in conjunction with the accompanying notes.

	Notes	Contributed equity	Convertible notes	Reserves	Retained profits	Total equity
		Attributable to owners of Aurizon Network Pty Ltd				
		$m	$m	$m	$m	$m
Balance at 1 July 2018		3.6	1,200.0	(13.2)	268.6	1,459.0
Profit for the six months		-	-	-	84.3	84.3
Other comprehensive income		-	-	(3.6)	-	(3.6)
Total comprehensive income for the six months		**-**	**-**	**(3.6)**	**84.3**	**80.7**
Transactions with owners in their capacity as owners:						
Dividends provided for or paid	2	-	-	-	(178.9)	(178.9)
Capital contribution from the parent for share-based payments		0.1	-	-	-	0.1
		0.1	-	-	(178.9)	(178.8)
Balance at 31 December 2018		**3.7**	**1,200.0**	**(16.8)**	**174.0**	**1,360.9**
Balance at 1 July 2017		3.9	1,200.0	(4.3)	632.9	1,832.5
Profit for the six months		-	-	-	121.7	121.7
Other comprehensive income		-	-	4.1	-	4.1
Total comprehensive income for the six months		**-**	**-**	**4.1**	**121.7**	**125.8**
Transactions with owners in their capacity as owners:						
Dividends provided for or paid	2	-	-	-	(482.8)	(482.8)
Capital distribution to the parent for share-based payments		(0.2)	-	-	-	(0.2)
		(0.2)	-	-	(482.8)	(483.0)
Balance at 31 December 2017		**3.7**	**1,200.0**	**(0.2)**	**271.8**	**1,475.3**

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

	31 December 2018 $m	31 December 2017 $m
Cash flows from operating activities		
Receipts from customers	**736.0**	761.5
Payments to suppliers and employees	**(300.5)**	(337.4)
Interest received	**0.1**	0.2
Income taxes paid	**(34.3)**	(28.4)
Net cash inflow from operating activities	**401.3**	395.9
Cash flows from investing activities		
Payments for property, plant and equipment	**(113.9)**	(147.3)
Payments for intangible assets	**(7.6)**	(9.9)
Interest paid on qualifying assets	**(1.7)**	(1.1)
Net cash (outflow) from investing activities	**(123.2)**	(158.3)
Cash flows from financing activities		
Proceeds from borrowings	**38.0**	225.0
Repayment of borrowings	**(70.0)**	(5.0)
Payment of transaction costs related to borrowings	**-**	(3.9)
Capital distribution to parent	**-**	(0.1)
Loans from related parties	**5.0**	81.0
Dividends paid to Company's shareholders (note 2(a))	**(178.9)**	(482.8)
Interest paid	**(73.0)**	(70.8)
Net cash (outflow) from financing activities	**(278.9)**	(256.6)
Net (decrease)/increase in cash and cash equivalents	**(0.8)**	(19.0)
Cash and cash equivalents at the beginning of the financial year	**2.2**	21.0
Cash and cash equivalents at end of the six months	**1.4**	2.0

The above consolidated statement of cash flows should be read in conjunction with the accompanying notes.

About this report

Corporate information

The financial statements of Aurizon Network Pty Ltd ("the Company" or “Aurizon Network”) for the six months ended 31 December 2018 are for the consolidated entity consisting of the Company and its subsidiaries (together referred to as "the Group").

Basis of preparation

This consolidated Interim Financial Report for the six-month reporting period ended 31 December 2018 has been prepared in accordance with Accounting Standard AASB 134 *Interim Financial Reporting*. Where necessary, comparative information has been restated to conform with changes in presentation in the current year.

This consolidated Interim Financial Report does not include all the notes of the type normally included in an annual financial report. Accordingly, this financial report is to be read in conjunction with the annual report of the Company for the year ended 30 June 2018. The annual report for the Company is available at www.aurizon.com.au.

The consolidated Interim Financial Report is presented in Australian dollars with all values rounded to the nearest hundred thousand dollars, unless otherwise stated, in accordance with ASIC Corporations (Rounding in Financial/Directors' Reports) Instrument 2016/191.

Key Events and transactions for the reporting period

The financial position and performance of the Group was particularly affected by the following events and transactions during the reporting period:

Access undertaking (UT5)

On 6 December 2018 the Queensland Competition Authority (QCA) issued a Final Decision in relation to the Company's 2017 Draft Access Undertaking (UT5). UT5 sets the Company's overall Maximum Allowable Revenue (MAR) for the regulatory period from 1 July 2017 to 30 June 2021. The Final Decision MAR for the regulatory period is $4.123 billion.

Network access revenue for the six month period to 31 December 2018 has been recognised as 50% of the UT5 Final Decision MAR. This has been adjusted for a FY18 revenue true-up relating to the over recovery of transitional tariffs in comparison to the UT5 Final Decision MAR in the comparative period.

It is estimated that the FY18 revenue true-up excluding GAPE is approximately $60.8 million of which $30.4 million has been recognised as a reduction to revenue in the six month period to 31 December 2018. The Company's assumption is that the true-up will be repaid based on FY19 total volumes and therefore the remaining amount is expected to be recognised in the second half of FY19.

Network access revenue for the comparative period was based on transitional tariffs (approved by the QCA) applied to railed volumes.

Comparative Period

Key events and transactions affecting the performance of the Group in the comparative period are disclosed within the Financial Report for the year ended 30 June 2018.

Results for the six months

In this section …

Results for the six months provides a breakdown of individual line items in the consolidated income statement that the directors consider most relevant.

1 Revenue

The Company recognises revenue from the provision of access to the Central Queensland Coal Network (CQCN) and other incidental services. Revenue is derived from the following major sources:

- Track access revenue comprises: Provision of access to, and operation and management of the CQCN.
- Other revenue comprises: Revenue from minor operations including access facilitation charges, revenue from telecommunications and items of a corporate nature.

	31 December 2018 $m	**31 December 2017 $m**
Revenue from continuing operations		
Services revenue		
Track access	**534.1**	577.0
Other revenue	**23.3**	30.6
	557.4	607.6

Capital management

In this section …

Capital management provides information about the capital management practices of the Group and shareholder returns for the six months and the Group's fair value disclosure for financial instruments.

2 Dividends

(a) Ordinary shares

	31 December 2018 $m	31 December 2017 $m
Final dividend for the year ended 30 June 2018 of $230,000 (2017: $3,510,000) per share, paid September 2018 (unfranked)	**23.0**	351.0
Interim dividend for the year ended 30 June 2019 of $1,559,000 (2018: $1,318,000) per share, paid October 2018 (unfranked)	**155.9**	131.8
	178.9	482.8

(b) Dividends not recognised at the end of the reporting period

	31 December 2018 $m	31 December 2017 $m
The directors have not declared the payment of any dividend since 31 December 2018. Subsequent to 31 December 2017, the directors declared the payment of an interim dividend of $368,000 per fully paid ordinary share, unfranked. The aggregate amount of the dividend paid on 22 March 2018 out of retained earnings, but not recognised as a liability at 31 December 2017 was:	**-**	36.8

3 Borrowings

	31 December 2018 $m	30 June 2018 $m
Current		
Unsecured		
Working capital facility	**89.0**	51.0
Loans from related parties	**5.0**	-
Total current borrowings	**94.0**	51.0
Non-current		
Unsecured		
Medium-term notes	**2,617.5**	2,552.1
Syndicated facilities	**690.0**	760.0
Capitalised borrowing costs	**(8.3)**	(9.6)
Total non-current borrowings	**3,299.2**	3,302.5
Total borrowings	**3,393.2**	3,353.5

The Company's bank debt facilities contain financial covenants. Both the bank debt facilities and medium-term notes contain general undertakings including negative pledge clauses which restrict the amount of security that the Company can provide over its assets in certain circumstances. The Company has complied with all required covenants and undertakings throughout the reporting period.

4 Fair value disclosure for financial instruments

Fair values of financial instruments

The carrying amounts and fair values of all of the Group's financial instruments which are not carried at an amount which approximates their fair value at 31 December 2018 and 30 June 2018 are shown in the following table.

The fair value of borrowings is estimated by discounting the future contractual cash flows at the current market interest rates that are available to Aurizon Network for similar financial instruments. For the period ended 31 December 2018, the borrowing rates were determined to be ranging from 2.8% to 4.6% depending on the type of borrowing (30 June 2018: 2.7% to 4.5%).

	Carrying value		Fair value	
	31 December 2018	**30 June 2018**	**31 December 2018**	**30 June 2018**
	$m	**$m**	**$m**	**$m**
Borrowings	**3,393.2**	3,353.5	**3,465.9**	3,490.7

Valuation hierarchy of financial instruments carried at fair value on a recurring basis

The Group measures and recognises the following assets and liabilities at fair value on a recurring basis:
- Forward exchange contracts
- Interest rate swaps (including cross currency interest rate swaps)

(a) Fair value hierarchy

Financial instruments carried at fair value may be grouped into three valuation categories:
- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

All of the Group's financial instruments measured at fair value are categorised as Level 2. There were no transfers between Levels 1, 2 and 3 fair value hierarchies during the current or prior six month period.

(b) Valuation techniques used to derive fair values

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) are determined using valuation techniques. These valuation techniques maximise the use of observable market data where available and rely as little as possible on entity specific estimates. If all significant inputs required to determine the fair value of an instrument are observable, the instrument is included in Level 2.

The fair value of forward foreign exchange contracts has been determined as the unrealised gain / loss at balance date by reference to market rates.

The fair value of cross currency interest rate swaps has been determined as the net present value of contracted cash flows.

The fair value of interest rate swaps has been determined as the net present value of contracted cash flows.

These values have been adjusted to reflect the credit risk of the Group and relevant counterparties. The future probable exposure method has been adopted for forward foreign exchange contracts, cross currency interest rate swaps and interest rate swaps and is applied to the estimated future cash flows to reflect the credit risk of the Group and relevant counterparties.

Other information

In this section …

Other information provides information on other items which require disclosure to comply with Australian Accounting Standards and other regulatory pronouncements.

5 Summary of significant accounting policies

The principal accounting policies adopted in the preparation of this consolidated Interim Financial Report are consistent with those of the previous financial year except for the adoption of new and amended standards as set out below. These policies have been consistently applied to both periods presented, unless otherwise stated. Where necessary, comparative information has been restated to conform with changes in presentation in the current year.

New and revised accounting standards and interpretations
AASB 15 *Revenue from Contracts with Customers* became applicable for the current reporting period and the Group changed its accounting policies and made reclassifications to comparatives as a result of prospectively adopting the standard. The impact of the adoption of AASB 15 *Revenue from Contracts with Customers* and the new accounting policy is disclosed in note 6.

AASB 9 *Financial Instruments* was early adopted by the Group from 1 July 2014.

Certain new accounting standards and interpretations have been published that are not mandatory for 30 June 2019 reporting periods and have not been early-adopted by the Group. The nature of the change and the potential impact is discussed further below.

AASB 16 *Leases* (mandatory for financial year beginning 1 July 2019)
Nature of change:
AASB 16 *Leases* addresses the recognition, measurement, presentation and disclosure of leases. The Group will adopt the standard on 1 July 2019.

The adoption of AASB 16 will result in almost all leases being recognised on the balance sheet, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The lease liability is measured at the present value of the lease payments that are not paid at the balance date, and is unwound over time using either the interest rate implicit in the lease repayments or the Group's incremental borrowing rate. The right-of-use asset comprises the initial lease liability amount, and initial direct costs incurred when entering into the lease less any lease incentives received. The right-of-use asset is depreciated over the term of the lease. The new standard replaces the Group's operating lease expense with an interest and depreciation expense.

Impact:
Management is continuing to assess the effects of applying the new standard on the Group's financial statements. The Group has elected to apply the "Modified Retrospective Approach" when transitioning to the new standard. Under this approach, the Group will not be required to restate the comparative information for its operating leases, as the right-of-use asset will be brought onto the balance sheet at the same time as the lease liability on transition date. For existing finance leases currently recognised under AASB 117, there will be a revaluation of existing lease liabilities recognised in the balance sheet with a corresponding adjustment to the right-of-use asset.

Work on understanding the impact of the new standard is well progressed and includes:

- Identification of the provisions of the standard which will most impact the Group;
- Establishing the population of lease contracts which will extend beyond 1 July 2019;
- Discount rate determination;
- Impact analysis and the calculation of the lease liability and right-of-use asset on transition;
- Review of system requirements; and
- Provision of training.

The adoption of AASB 16 by the Group on 1 July 2019 is not expected to have a material impact on profit before income tax in the financial year ending 30 June 2020.

6 Changes in accounting policies

(a) AASB 15 *Revenue from Contracts with Customers* – Impact of adoption
The Group has adopted AASB 15 *Revenue from Contracts with Customers* from 1 July 2018 which has not resulted in any adjustments to amounts previously recognised in the financial statements. The accounting policy has been updated to reflect the wording changes in AASB 15.

In accordance with the transition provisions in AASB 15, the Group has adopted the new rules retrospectively with the cumulative effect recognised at the date of initial application. There was no impact on the Group's retained earnings as at 1 July 2018 being the date of initial application.

6 Changes in accounting policies (continued)

(b) Accounting policies
The Group recognises revenue as the relevant performance obligations are satisfied. Revenue includes the provision of track access services as described below.

(i) Track access
Track access revenue includes revenue from regulated access services and revenue from non-regulated services. Track access revenue is generated from the provision of access to, and operation of, the Central Queensland Coal Network (CQCN). Access revenue is recognised as the relevant performance obligations are satisfied, being the provision of access to the rail network.

Approved Access Undertaking
Track access revenue is recognised as track access is provided and is measured on a number of operating parameters including volumes hauled applied to regulator approved tariffs. The tariffs charged are determined with reference to the total allowable revenue, applied to the regulatory approved annual volume forecast for each system. At each balance date, track access revenue and receivables include an amount of revenue for which performance obligations have been met under the respective contract but have not yet settled. The Group has an unconditional right to receive this consideration once the performance obligation is satisfied and therefore a trade receivable is recognised for these amounts.

Where annual volumes railed are less than the regulatory forecast, Take or Pay may trigger. Take or Pay is recognised as a receivable in the year that the contractual railings were not achieved as the related performance obligations have been satisfied.

The majority of access revenue is subject to a revenue cap mechanism that serves to ensure the network recovers its system allowable revenue over the regulatory period. A revenue cap event results in the under or over recovery of regulatory access revenues (net of Take-or-Pay revenue) for a financial year being recognised in the accounting revenues in the second financial year following the event through an adjusted tariff.

Transitional Tariff Period
During a transitional tariff period, track access revenue is recognised and measured based on the most relevant and reliable information available. Refer to note 7 for additional information.

A contract liability is recorded for revenue received in advance of satisfying a performance obligation and is recognised over the term of the contract.

7 Critical accounting estimates and judgements

A number of critical accounting estimates and judgements were disclosed in the 30 June 2018 financial report. Included within those judgement and estimates are the following which have particular relevance to the Interim Financial Report.

Access revenue

Network access revenue for the six month period to 31 December 2018 has been recognised as 50% of the UT5 Final Decision MAR. This has been adjusted for a FY18 revenue true-up relating to the over recovery of transitional tariffs in comparison to the UT5 Final Decision MAR in the comparative period.

It is estimated that the FY18 revenue true-up excluding GAPE is approximately $60.8 million of which $30.4 million has been recognised as a reduction to revenue in the six month period to 31 December 2018. The Company's assumption is that the true-up will be repaid based on FY19 total volumes and therefore the remaining amount is expected to be recognised in the second half of FY19.

There are a number of assumptions that underpin access revenue recognised for the six month period to 31 December 2018 including volumes and the repayment mechanism of prior year true-ups. There is a risk that these assumptions will be different from the final approved UT5 Access Undertaking.

Network access revenue for the comparative period was based on transitional tariffs (approved by the QCA) applied to railed volumes.

Unrecognised items

In this section …

Unrecognised items provide information about items that are not recognised in the financial statements but could potentially have a significant impact on the Group's financial position and performance.

8 Contingencies

Issues relating to common law claims and product warranties are dealt with as they arise. There have been no material changes in contingent assets or liabilities since 30 June 2018.

9 Events occurring after the reporting period

There have been no matters or circumstances occurring subsequent to the reporting period that have significantly affected, or may significantly affect, the operations of the Group, the results of those operations or the state of affairs of the Group.

In accordance with a resolution of the directors of the Company, I state that:

In the opinion of the directors of the Company:

(a) the financial statements and notes set out on pages 3 to 19
   (i) comply with Accounting Standards; and
   (ii) give a true and fair view of the consolidated entity's financial position as at 31 December 2018 and of its performance for the six months ended on that date, and

(b) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

A Harding
Director

Brisbane QLD
11 February 2019

Independent auditor's review report to the members of Aurizon Network Pty Ltd

Report on the Half-Year Financial Report

We have reviewed the accompanying half-year financial report of Aurizon Network Pty Ltd (the Company), which comprises the consolidated balance sheet as at 31 December 2018, the consolidated statement of comprehensive income, consolidated statement of changes in equity, consolidated statement of cash flows and consolidated income statement for the half-year ended on that date, selected other explanatory notes and the directors' declaration for Aurizon Network Pty Ltd. The Group comprises the Company and the entities it controlled during that half-year.

Directors' responsibility for the half-year financial report

The directors of the Company are responsible for the preparation and fair presentation of the half-year financial report in accordance with the accounting policies as described in the notes to the financial statements and have determined that the accounting policies in the notes, which form part of the financial report, are appropriate to meet the needs of the members and internal purposes. The directors are also responsible for such internal control as the directors determine is necessary to enable the preparation of the half-year financial report that is free from material misstatement whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express a conclusion on the half-year financial report based on our review. We conducted our review in accordance with Australian Auditing Standard on Review Engagements ASRE 2410 *Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, anything has come to our attention that causes us to believe that the half-year financial report is not presented fairly, in all material respects, in accordance with the accounting policies as described in the notes to the financial statements. As the auditor of Aurizon Network Pty Ltd, ASRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half-year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. It also includes reading the other information included with the half-year financial report to determine whether it contains any material inconsistencies with the half-year financial report. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Independence

In conducting our review, we have complied with the independence requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants*.

Conclusion

Based on our review, which is not an audit, nothing has come to our attention that causes us to believe that the half-year financial report of Aurizon Network Pty Ltd does not present fairly, in all material respects, the consolidated entity's financial position as at 31 December 2018 and its performance for the half-year ended on that date, in accordance with the accounting policies as described in the notes to the financial statements.

PricewaterhouseCoopers

PricewaterhouseCoopers

Tim Allman
Partner

Brisbane
11 February 2019