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PRESENTATION

Andrew T. Harding *- Aurizon Holdings Limited - MD, CEO & Director*

Good morning, and welcome to the interim results for financial year 2018 for Aurizon. In the room with me today are the following members of the executive team: Pam Bains, CFO and Group Executive Strategy; Ed McKeiver, Group Executive Coal; Clay McDonald, Group Executive Bulk; Michael Riches, Group Executive Network. They're available for questions at the end, after Pam and I have finished the presentation.

Before we get started, you will notice a change to past presentations with more key information in the front section. We did this because there is a lot going on, and I wanted to update you on the priorities for the group and each business unit as they now exist under the new structure. Each business has its own set of priorities and challenges, and how we respond is critical to the success of the group.

As usual, first, we will start with safety. As indicated 6 months ago, we have revised our metrics to include contractors and all restricted work injuries in our recordable injuries. This was to ensure the definition is consistent with the best practice, and the numbers you see here are on this basis, including higher numbers for the prior years.

We have seen a deterioration in the performance since June last year, which is largely a reflection of 2 issues. The first, our systems and processes were not previously set up to record all contractor injuries so although we have restated the prior year's data, we have not been able to capture all historic injuries.

Second, there has been an underlying increase in strain-related injuries to our employees. The result itself is disappointing, but analyzing the underlying root cause has allowed us to identify new areas of focus for our safety journey to help drive further improvements. This includes improving the processes around manual handling tasks and strengthening the processes around the interaction, including induction of contractors in the business. As I highlighted at the FY '17 results day, improvement in the new metric will be harder and will focus the business on a larger safety improvement at Aurizon.

Before I run through some high-level comments about the financial results, I wanted to give you an update on the key priorities I have identified -- I had identified 1 year ago after joining Aurizon. There's been a lot of activity in Aurizon that is aligned to these priorities and where success delivers significant value to our investors. Later on, I will talk through the more forward-looking aspect of the priorities, including financial guidance.

On capital management, we promised to return surplus capital to investors, and I am very pleased that the buyback announced in August is already 75% complete, with the balance to be completed in the second half. You will also see the decision today to pay the interim dividend on underlying net profit after tax for the continuing operations, delivering a 3% increase.

Good progress has been made against the outcomes of the Freight review, with the interstate business closed prior to Christmas, and we continue to safely and effectively run the Queensland operations in advance of the sale later this half, which remains subject to regulatory approval. The remaining Bulk business is seeing the early signs of success in the turnaround plan as we improve earnings and returns as I will go through later.

The transformation program is progressing well with $42 million in sustainable benefits delivered in the half, and we have now achieved more than $300 million since FY 2016. We are targeting a further $40 million in the second half. And when combined with the Intermodal losses foregone of $48 million, this should put us slightly ahead of the 3-year target of $380 million.

The UT5 Draft Decision was delivered by the QCA and clearly was unacceptable, demonstrating their lack of understanding or care about risk and commercial reality. Addressing this is a priority, and we have already taken action, which I'll talk about shortly.

Now turning to the half year highlights. After the challenges of 2017, which included floods and impairments, this year has enabled the Aurizon team to focus on the tasks at hand in delivering for our customers. It's a solid financial result despite underlying EBIT being 5% lower at $485 million as this was due to the non-recurrence of network true-ups in the prior year relating to the finalization of UT4.

As you can see from the chart, there was EBIT growth for the Coal and Bulk businesses, but this was more than offset by the decrease in Network. These businesses have continued to benefit from the transformation program, whilst in Coal, we also saw a strong volume performance.

Volumes grew 4% in Above Rail, Coal and Network, delivered -- and -- sorry in Above Rail Coal and Network delivered an all-time record tonnage number, while the decline in Bulk volumes was in line with expectations given the decision to exit the Mount Isa freighter early in 2017. With no underlying adjustments for the continuing operations, statutory NPAT was up strongly to $282 million.

Free cash flow performance continues to be strong, although it has decreased for the continuing operations due to $98 million in cash proceeds received last year for the sale of the Moorebank investment. As this was an investment and not part of the Intermodal operations, it is classified as part of the continuing operations.

And finally, as previously noted, the focus on shareholder returns has continued with the interim dividend up 3%, and we have made excellent progress on the buyback commitment.

Turning to the Coal business. We continue to operate in strong commodity price environment for our customers, and that is helping demand and keeping volumes strong. I wanted to talk about 3 things this morning: an update on the competitive end market for Aurizon; our customers; and finally, the broader coal market with a focus on the continued strength of Australian coal in a global context.

We have had excellent success in the contracting space recently. And today, we are announcing 3 new agreements, including 2 greenfield mines: MACH Energy's Mt Pleasant Mine in Hunter Valley and QCoal's Byerwen Mine in Queensland, both of which commenced railings this year. It is really good for the industry to see new tonnes coming to the market.

Competing for and winning contracts is not easy, and we have seen very keenly contested tender processes in Queensland and New South Wales that is putting some downward pressure on contract prices. This pressure highlights the importance of continuing to improve productivity and efficiencies, which is valuable to our customers and which will ultimately improve our own cost base and margins.

Flexibility has been as important as pricing contracts recently, and that means a less rigid approach on things such as capacity charge levels, volume nominations, and in some cases, contract wins. Despite this, weighted average contract life remains a healthy, very healthy 9.4 years, and all customers are operating at positive cash margins given the strong coal prices.

We remain confident about the outlook for Australian coal export volume. On the demand side, Australia's largest metallurgical coal trading partner, India, reached annual crude steel production of over 100 million tonnes for the first time in 2017. Investment in infrastructure and manufacturing in India will continue to drive demand for steel and, therefore, metallurgical coal.

Recalling that over 95% of Australian thermal coal exports are destined for Asia, it is this region rather than global consumption that continues to add coal-fired energy generation capacity. Although we, of course, recognize that renewable energy will increase in the energy mix over the long term, thermal coal capacity will remain and is expected to grow in absolute terms in key export nations like Australia.

For both coal types, the quality of Australian coal and the cost competitiveness, including access to reliable rail infrastructure, provides confidence that Australia will continue to be a significant contributor to seaborne supply. As a result, we expect to see Australian coal export volume growth of 1% to 2% CAGR over the next decade for both coal types.

Moving now to comment on the Bulk business. There has been good progress in the Bulk business, and things are on track for the turnaround plan. However, it is early days, but the team is focused on ensuring performance is maintained.

As a reminder, the original Freight Review identified 17 individual hauls for the Bulk business. Of the original 17 hauls, 5 were classified as retained, 7 transformed and 5 were exit. And I wanted to give a brief update on these 3 groups with an emphasis on the middle group as that is key to ensuring the success of this business.

The contracts in the transform bucket require a combination of cost reductions from the transformation program and also improved commercial terms, and there are 3 examples I wanted to talk about today.

Cement Australia, we have recently secured a 10-year extension for this limestone haul in Gladstone. MMG, during this period, we commenced railings for this customer on a revised contract with zinc and lead concentrate now being shipped in containers on the Mount Isa corridor and the Kalgoorlie Freighter. This is a great example of an improved operational solution, driving efficiency and lowering costs.

Previously, we had to break the train apart at Forrestfield as a full consist could not fit into the end destination, Kwinana, where most customers are located. We upgraded the track and built minor rail extensions at Kwinana, which enables train separation to occur much closer to the customers, which is more operationally efficient.

A small capital investment with a quick payback, in combination with increasing the customer utilization in train, is paying dividends.

These 3 actions have enabled these hauls to move into the retain bucket, although it is not a case of job done, with further transformation initiatives needed to deliver value. The remaining transform hauls I have not talked about all have various cost initiatives being implemented and commercial discussions with customers, which are subject to various time frames. Therefore, this group remains a work in progress.

The 5 original contracts in the retain bucket will benefit from broader transformation and the improved customer focus that comes from the new structure.

And finally, of the 5 exits, we have managed out 4 already. The remaining contract has a further 3 years to run until it ends in early FY '22 due to onerous early termination provisions. As we believe this contract has no prospects of commercial improvement in this time frame, we will not be seeking to renegotiate it.

In addition, there are further 3 iron ore hauls in the new bulk portfolio, including Cliffs. We note the news from this customer about shutting down their operations potentially this year, which is a few years earlier than expected. At this stage, we have not received formal notification about this, and they continue to rail according to plan. The contract has provisions to deal with early termination should the customer elect to do this.

Turning now to Network. While Network's strong operating performance continued during the half, it was overshadowed in late December by the Queensland Competition Authority's UT5 Draft Decision. The message for me is simple. This draft is extremely disappointing, economically irresponsible and in large parts just plain wrong. Despite volumes of evidence and opposing views from investors, independent experts and analysts and rating agencies, the QCA believes Aurizon's Central Queensland Coal Network is the lowest risk regulated asset in Australia, and therefore should earn the lowest return.

In addition, we cannot reconcile the QCA's decision that Network's WACC should be 5.41%, compared to 6.3% recommended by the ACCC just 8 months prior for the government-owned Hunter Valley Rail Network, an asset which many of our customers regard as having a lower risk profile. The Draft Decision reflects a clear approach by the QCA to drive maintenance to the lowest possible cost regardless of the impact on the supply chain and consequential reduction in volumes. The QCA believes that we should spend less than in the UT4 period even though we have an additional $1 billion in assets to maintain, and the QCA themselves forecast 15% volume growth over the 4 years of UT5.

Because of the retrospective -- because of the retrospectivity of UT5, 2 weeks ago, we started to align our operating and maintenance practices to the QCA Draft Decision. An example of aligning practices to the QCA's Draft Decision on maintenance is the operation of the ballast undercutter, which replaces the ballast which sits under the rail. Our current practices are designed to facilitate throughput by prioritizing the running of coal services, whilst undertaking this maintenance work. The QCA Draft Decision states that maintenance should take priority over coal services as that is the lowest cost.

Accordingly, there will no longer be any flexibility in the maintenance schedule to allow trains through during maintenance periods to ensure our costs are aligned to the QCA allowance. Whilst this practice reduces costs, it will also have a significant impact on volumes.

Aurizon Network is also reassessing how we manage risk in a lower return environment. We expect further changes in operating practices to ensure our risk tolerance is aligned with our return. An example of operating practices that have risk associated with them which are being assessed is the treatment of rail breaks. Currently, when a rail breaks, we would generally implement a temporary fix by clamping the rail, which takes a shorter time to complete than a full repair, allowing trains to continue to run. We will then generally be able to wait for a scheduled maintenance shutdown to perform the full repair. This places operational risk on the network, given we have a temporary repair in place, but ensures the system keeps running so coal trains can get to the port. We will be assessing that practice to understand whether, in an environment where we will be less inclined to take risk on long-term track reliability, we may need to complete permanent repairs as the preferred approach. These repairs would likely not be able to be completed without a significant greater impact on throughput.

Overall, the QCA's approach would appear to have limited regard to the operational requirements and economic importance of Queensland's coal export supply chain. It demonstrates their formulaic and theoretical approach and lack of understanding of the commercial drivers and risks of this business and what the impact will be to jobs and regional economies and Queensland's share of the global coal market.

We estimate that aligning to the QCA Draft Decision will initially reduce total system throughput by about 20 million tonnes per year, which is greater than the 16 million tonnes impact from Cyclone Debbie in 2017. As we reluctantly implement further changes in the coming months, again to align our operating practices with the QCA Draft Decision, this will see network capacity further reduced likely by a significant amount.

This is not a decision we've taken lightly. But Aurizon Network has little choice but to implement these changes now because of the retrospectivity of UT5, which is in effect from July last year. We are very aware that the impact to network throughput will have a significant impact on customers and other industry stakeholders, including our own Above Rail coal business. In the meantime, we will continue to progress our response to the QCA, which is due by 12 March.

Turning to the next slide, this chart shows you quite clearly the WACC, as proposed by the QCA in the UT5 Draft Decision, has concluded that the CQCN is one of the lowest risk regulated assets in Australia. Anyone with even a basic working knowledge of the system would know this is not the case. What is even more apparent is the disparity in returns for other Australian-regulated rail infrastructure being ARTC, Arc., New South Wales Rail and Pilbara Railway, and we would note all of these decisions occurred within the last year.

Pam will shortly run through some of the numbers around Intermodal, which is being treated as a discontinued operation in our accounts. I wanted to provide some detail on implementing the decision we have made, which have so far proceeded to plan.

The Interstate business operated its last service in December, and we are in the process of transferring assets and people into growth areas, including the Hunter Valley coal. Some 40 employees have been transferred, and 6 locomotives already made their way across the country to the Hunter Valley. This enables us to complete for new contracts now and in the future as we did not previously have surplus assets to deploy there.

The execution of the Interstate shutdown has resulted in Aurizon exceeding the value assumptions that underpins the decision. For the remaining sale of the Queensland business and Acacia Ridge, we note that the ACCC was due to comment by 1 February, but this is being pushed out due to requests for new information.

Aurizon is of the view that the ACCC should approve the transactions, but we will have to wait for their decision sometime later this month. It will either be to clear the transaction at that time or more likely issue a statement of issues, inviting further submissions from the parties on areas of concern. If we are not able to gain ACCC approval for the transaction, then we will close the Queensland business as we have done with Interstate.

And now I will hand over to Pam.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Thank you, Andrew, and good morning to everyone on the call. I will start with an overview of Aurizon's financial performance for the half, noting that the half now reflects the new business unit model, which was implemented on 1st of July of last year. We provided the market with prior period -- restated comparatives in December.

It's also worth noting that as part of the process of resetting segments, we also performed a full review of our cost allocation methodology, which had not been revised for a few years, to ensure a more accurate reflection of BU performance, and this will continue to be refined.

In August last year, we announced the intention to exit the Intermodal business through a combination of closure of the Interstate business and the sale of Acacia Ridge and Intermodal Queensland. Hence, the result is presented on a continuing basis, that is it excludes Intermodal, which is disclosed as discontinuing. We executed the closure on time and ahead of expectations, and I'll provide an update on closure costs a little later.

Moving to the result. Overall, a solid no-surprises performance, in line with guidance provided. Revenue and EBIT for the continuing operation decreased by 3% and 5%, respectively. A key driver of the performance against the prior half is the UT4 one-off benefit not repeated in this half, as Andrew mentioned, and lower volumes in Bulk. This has been partly offset by increased Coal revenue from growth volumes.

Operating costs reduced by $11 million, supported by transformation of $42 million, offset by redundancy costs taken above the line of $15 million, net incremental costs from increased volumes in Coal, partly offset by reduced volumes in Bulk totaling $8 million and CPI impacts of $11 million.

Depreciation reduced by $18 million as a result of the impairments in Bulk in FY '17 of $23 million, offset by small increases in Coal and Network, totaling $5 million. Statutory EBIT for the continuing operations improved by $129 million as there were no significant items this half compared to the prior half, which included $156 million.

Due to the closure and sale of the Intermodal business, which has been classified as discontinuing, we did have $77 million in significant items, which comprise $5 million in asset impairments, $60 million of closure costs and redundancy costs of $12 million. Net profit after tax declined 5%, in line with the EBIT decline.

The board has declared an interim dividend of $0.14 per share franked at 50%. This equates to a payout ratio of 100% of underlying net profit after tax on a continuing basis and reflects an increase from the FY '17 interim dividend of 3%. This is considered appropriate for the half year given that transitional tariffs for Network have now been approved by the QCA for FY '18.

Moving to the Coal business unit. EBIT increased from $218 million to $223 million. Improved volumes, both in Central Queensland Coal Network of 2% and New South Wales Southeast Queensland of 12% have driven increased revenue.

CQCN has seen strong railings across Goonyella and Newlands, and Fitzroy and Batchfire also commenced railing in the half. New South Wales volume uplift is largely due to the commencement of the AGL contract in July of '17. Revenue quality reduced with improved contract utilization, which increased 2 percentage points up against the prior half.

Coal delivered transformation of $27 million in the half, and this was offset by costs supporting volume growth of $20 million, primarily labor; wages and consumable escalation, $6 million; redundancy costs taken above the line of $7 million; and the cost of 2 derailments of $2 million.

There was a modest increase in depreciation of $2 million, largely due to a new rolling stock in the Hunter Valley. It's worth noting, with the transfer of locos following the closure of Intermodal Interstate to Coal, we expect the second half depreciation to be slightly higher. So overall, a positive result from Coal in a market showing improvement in demand, higher contract utilization and some competitive pricing.

In relation to Bulk, we continue our journey of transformation through a continuous review of both revenue contracts and cost to serve. Underlying EBIT increased $18 million to $20 million due to a combination of cost reduction and lower depreciation from impairments in the prior year. This was partially offset by 6% lower volumes, 14% in NTK terms as a result of lower volumes in the East, with the cessation of the Mount Isa Freighter in January of 2017 and lower grain volumes. Grain volumes were impacted by dry conditions with supply being directed to the domestic market. Aurizon only hauls for export hauls.

In the West, iron ore volumes, due to production issues with one of our customers, offset by higher volumes in bauxite and growth on the Kalgoorlie Freighter. Hence, revenue reduced by $23 million due to the Mount Isa Freighter closure, lower iron ore volumes and also lower grain volumes in both Queensland and New South Wales. Revenue quality is up $6 million in part due to lower contract utilization.

Transformation in Bulk totaled $11 million in the half. As a result of the impairment in the prior year, depreciation has decreased $23 million. This has been offset in part by $5 million impairment expense, which is included in operating costs to provide a net depreciation benefit of $18 million. Other includes removal of costs associated with Mount Isa Freighter of $12 million, partly offset by cost escalation and redundancy costs totaling $7 million.

In summary, the Bulk results clearly highlights the transformation work being done to turn this business around, but with continuing challenges on the top line.

The result for Network should be no surprise, except for the UT5 Draft Decision, which was extremely disappointed -- disappointing, as Andrew highlighted. EBIT decreased, as expected, from $293 million to $249 million in the half due to prior period UT4-related adjustments.

We communicated guidance on the basis of transitional tariffs, and the QCA has since approved the extension to 30 June 2018. Accordingly, we do not expect any under or overrecovery to the final UT5 decision to impact FY '18. The transitional tariff extension also includes recovery of $17 million in relation to costs of repair for damage caused by Cyclone Debbie.

Volumes were strong in Network, hitting a record half. Revenue in the prior period includes $45 million non-reoccurring UT4 true-ups and a further true-up of $12 million for GAPE, non-regulatory revenue and rebates. This relates to revenue that was under-collected in prior years, in 2014 and 2015, awaiting finalization of UT4.

In the half, there was a reduction of $11 million due to the revenue cap adjustment for FY '16, which was an over-collection in that year. Higher recoveries for energy costs included in revenue of $17 million. However, there is a corresponding offset in energy cost expense as this is a pass-through item.

Other revenue in the prior half includes one-off receipt of $15 million for Bandanna bank guarantee and insurance recoveries of $6 million. This was offset in part by a $10 million bank guarantee in relation to Caledon coal received this half. Both bank guarantees were WIRP fee-related.

Operating costs, including depreciation, have improved $20 million or 5%, largely due to reduced consumable costs of $27 million with the reduction in corporate costs due to the non-recurrence of UT4 corporate cost true-up, lower operating costs from Minerva and Blackwater power systems. This was partly offset by a $5 million increase in labor costs mainly due to escalation and $3 million net increase in energy costs.

Depreciation increased modestly by $3 million due to higher asset renewals and vehicle replacement. The result for Network, while showing a decline, was very much in line with expectations due to prior year adjustments. The key focus for Network, which Andrew talked about at length, is UT5. So I'll just leave it there.

Intermodal. Notwithstanding the Intermodal Interstate closure in December, the EBIT loss for Intermodal was flat at $24 million with 12% lower revenues mainly on the back of reduced volumes with the ramp down in the Interstate business, partly offset by a 6% improvement in operating costs and an $8 million decrease in depreciation, which was the impact of the prior period impairment.

Significant items of $77 million have been recognized with most costs to be paid in the second half. During the first half, a provision has been made for redundancies of $12 million, representing 166 FTEs, asset write-downs of $5 million and other costs, including contract, lease and supplier exit costs of $60 million. The accrual represents Aurizon's current forecast for the closure costs at this point in time.

Free cash flow has improved $55 million, largely due to the $40 million deposit received for the sale of Acacia Ridge and Intermodal Queensland. We did -- we expect this position to unwind in the second half as the costs of closure are paid.

Moving to capital expenditure. We previously provided guidance for FY '18 and FY '19 at approximately $525 million and $500 million, respectively, which excluded any additional growth CapEx except for AGL and Whitehaven wagons. We now expect capital spend for the year to be approximately $500 million. This is despite a forecast increase in overall growth capital, mainly in coal for New South Wales growth volumes. This is offset by lower-than-forecast spend in the first half and a forecast reduction in network spend in the second half as we assess the CapEx program in the context of the proposed lower return in the UT5 Draft Decision. Future network CapEx will be reviewed in light of the UT5 Draft Decision, specifically FY '19 and FY '20, to ensure spend is in line with the allowance provided and reflects the risk profile assumed by the regulator.

In terms of overall cash flow, our focus remains on driving strong free cash flow generation. The decline in free cash flow of 11% or $42 million against the prior period is largely due to the proceeds from the sale of Moorebank, $98 million, which was included in the previous half. Net cash from operations was up 10% in the half, driven by lower taxes paid.

From a group perspective, we expect cash flow to be impacted in the second half with the payment of closure cost for the Intermodal Interstate business. We note that the future cash benefit of the Intermodal transaction will provide further upside in FY '19 from both the remainder of the sale proceeds of $185 million, subject to regulatory approval, and proceeds from the sale of Forrestfield.

Finally, before I hand back to Andrew, a quick update on funding. Aurizon's debt management strategy continues to be diversifying the debt investor base and increasing average debt tenor. Weighted average debt maturity at 31st of December was 5.1 years. Interest costs reduced from 5.1% to 4.5%. The decrease in funding costs of 60 basis points was due to the roll-off of the UT4 interest rate swaps in June '17, which was subsequently replaced with UT5 interest rate swaps.

During the half, in November '17, Aurizon Network repriced and extended an existing $525 million bank facility, with maturity extended to 2023 and tranche size reduced slightly to $500 million. As you can see, Aurizon retains minimal refinancing risk, and our credit rating with S&P and Moody's remains a BBB+ with stable outlook for both Group and Network.

In August, I talked about capital structure and what we deemed to be an appropriate target gearing for the group, taking into account the ability to meet credit metrics, market conditions, and in particular, the uncertainty of the UT5 decision. If the UT5 Draft Decision is imposed as it currently stands, Aurizon Network will not be able to meet its credit metrics, partly due to a difference of opinion on risk profile between the QCA and the international credit rating agencies. This is something that the QCA themselves recognize in the Draft Decision. This creates a challenge for Aurizon as it is not possible to gear the Network business in line with the regulatory assumptions without breaching the credit metrics despite the fact that the regulatory WACC assumes a BBB+ credit rating. This will result in either an inefficient capital structure or a downgrade in the credit rating.

The management team, in consultation with the board, will consider what is an appropriate response and credit rating after the final decision.

Thank you, and now I'll hand back to Andrew.

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Thanks, Pam. Turning now to the financial outlook. EBIT guidance is unchanged despite the strong first half performance. This is due to the reduction in Above Rail coal volumes to 210 million to 220 million tonnes from the likely impact of implementing revised operating and maintenance practices in Network to align with the UT5 Draft Decision. As usual, this is subject to the normal assumptions, in particular around weather.

And finally, to key takeaways. As I've highlighted during today's presentation, we have completed or are well down the path of completing most of the initial list of focus areas I talked about at my first results presentation only 1 year ago. I fully intend to complete the remainder of the list.

As you heard on UT5, we are aligning the way we operate and maintain the network to the QCA's view on risk and efficiency due to the retrospectivity of the decision. This will impact the whole supply chain, including our own business. We will continue to engage with all stakeholders in advance of the response due on 12 March.

The one thing I have not addressed today is strategy. But based on all the decisions you've seen over the past year, you can get a very good idea of where we are heading. Safety remains our core value, and transformation and improving productivity will continue to feature at Aurizon for some time yet in order to create sustainable value.

We're also interested in exploring appropriate growth opportunities where they exist, such as our interest in WICET. This is a quality coal asset that is already operating and is a natural extension of our own infrastructure, but has a capital and port tariff structure that needs to be addressed, something we think we have a solution for. We remain in early discussions with the many stakeholders that are party to this proposed transaction.

So we will talk in more detail about these things at an investor update in June this year. Do not expect something drastically different or new compared to all the decisions and actions you've seen this company make over the past year. It will offer a good opportunity to hear about the work in more detail and to meet the management team accountable for delivering the results.

Thank you very much, and now over to some questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Simon Mitchell from UBS Investment Bank.

Simon A. Mitchell - *UBS Investment Bank, Research Division - MD and Head of Research for Australia and New Zealand*

Andrew, just regarding the UT5 Draft Decision. I imagine you've had engagement with the regulator and customers since that decision came out, and particularly given the changes in maintenance practices that you talked about today. Can you give some insight into what the reaction has been to those discussions?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So you -- Simon, yes, you're correct. We've obviously had a lot of engagement with all the various stakeholders involved and around that decision. What would probably be best is if I hand over to Mike Riches, who's head of the Network, and he can give you some detail on what's happened.

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

Thanks, Andrew. In relation to the regulator, we've certainly spoken to them and, as Andrew and Pam have indicated, expressed our extreme disappointment with the decision and the approach they have adopted with the decision. We will continue the process that is set out in the QCA Act to put a submission in strongly rejecting a lot of the positions that the QCA have put. That submission is due on the 12th of March. In relation to the customers, we continue to engage with them to indicate the changes that we will need to make across the business, both in terms of our maintenance practices, and more generally, around risk for the business. And we'll continue to impress upon them, obviously, the impact associated with those changes.

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Okay. Thanks, Michael.

Simon A. Mitchell - *UBS Investment Bank, Research Division - MD and Head of Research for Australia and New Zealand*

Okay. And just secondly, on Network. Just interested in the cost base in the first half that I think it came in about $210 million, excluding depreciation. Is that -- would that be a go-forward sustainable rate? And also, perhaps if you can quantify in some way the benefit from the changes to maintenance practice that you talked about today?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Pam, I'd like you to answer that question.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

No problem. I think it's difficult at this stage to assume either way until we've worked through the specific initiatives that we're proposing and hence work through the cost of those and difficult to say at this stage.

Simon A. Mitchell - *UBS Investment Bank, Research Division - MD and Head of Research for Australia and New Zealand*

Okay. But just on the cost base in the first half, if we just put aside for one moment the maintenance practice changes, the cost base in the first half, there's nothing unusual in that which would mean it's not sustainable?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

No.

Simon A. Mitchell - *UBS Investment Bank, Research Division - MD and Head of Research for Australia and New Zealand*

Okay. And just lastly for me, just one final question. The additional 20 million tonnes per annum, roughly, under the new -- 3 new contracts, looks like most of that comes through in FY '19 with your contracted tonnage. That's up from about 200 million tonnes to 250 million. Do we expect any negative impact on revenue quality in coal as a result of those contracts?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So I will hand that to Ed in a second to give you some more detail on that. But one thing to understand is there is a ramp-up profile associated with those contract wins, which is important to understand. I'll hand it over to Ed.

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Yes. So Simon, thank you for the question. It's probably too early to tell in relation to the impact that it's -- we're still working through the details. And then as Andrew has said, given the ramp up volumes, it will depend on where the capacity degrade occurs.

Operator

Your next question comes from Anthony Moulder from CLSA.

Anthony Moulder - *CLSA Limited, Research Division - Analyst*

Just if I can touch back on one of the earlier questions. The customer engagement through UT5, I think you were hoping to get some support from customers that you wouldn't have to change maintenance practices, et cetera, back to the QCA. And do I hear from this that the customers generally have been unsupportive of that view? Or is -- I can't imagine that you come to this conclusion of taking capacity out of the Network lightly.

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So, Anthony, thanks very much for the question. I mean, look, there's a number of factors that are worth understanding. I'll point to our customer engagement scores, sadly, were at their highest point ever in December, and you can see a massive ramp up in the scores month by month since Michael Riches joined the company, massively focused on customer satisfaction. So keenly as I am focused on delivering for the customers. The important thing here is to understand this is a regulated business and you've got a regulator that actually basically calls the decisions. And the Draft Decision, if I was to describe it is, it's not a thought bubble. It's not some guys that get together in a pub after work and draw up an idea -- a way of working on a beer coaster. It's something that's actually -- had taken many, many months to actually deliberate on. They've spent millions of dollars -- because I've seen the invoices -- actually developing the position. And at the endpoint of this is, actually, they're just fundamentally wrong. The actual statement in the QCA Draft Decision is a train service that will, should, never interfere with a planned possession, i.e. maintenance. So they're very clear. We took to them and we gave them tours of the operation, and we've taken them in one-on-one, 2-on-2 explanations of great detail technical level of what's going on. And at the end, equally, the customers make submissions about in some great detail also. The end result of this vast deliberation and expensive deliberation is the Draft Decision. The Draft Decision is applied retrospectively. So I'm already most of the way through the first year of this decision being impacted, and it's costing us a great deal of money. So we have to act very quickly to actually position ourselves with the Draft Decision. If you look at the history and it's just data, the history of the difference between QCA Draft Decisions and final decisions, irrespective of submissions made by anyone, the difference is minimal. Actually, it's trivial. And so while I am optimistic that I will continue with Michael to work very hard through this normal process to get a sensible outcome, I can't assume, based on history, that a sensible outcome has any chance of actually being delivered. So what I have to do to minimize the risk to the business is undertake what I have explained to you, knowing that as somebody who has worked for a mining company for a long time and has run many coal mines actually that this -- the QCA decision is fundamentally flawed. I hope that helps you understand the situation.

Anthony Moulder - *CLSA Limited, Research Division - Analyst*

I think it does and I have probably come to the same conclusion that you do as we all do. But I guess, I'm still surprised as to why the customers haven't come to a similar position to be perhaps more supportive back to the QCA before the decision to pull down tonnages in the Network. I guess that's my surprise.

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

If I can maybe help a little bit there. I think, obviously, customers -- the coal mining industry goes through cycles, they've just gone through a cycle of reducing their costs. They're always looking at trying to achieve the lowest cost outcome. I think that was the position of their submission is to try and achieve the most efficient costs. I guess, what we'd say is the QCA -- I don't think they've taken into account the miners' submissions, our submissions. They've taken a particular view which has delivered an outcome that has resulted in a significant degradation to volumes through the supply chain. We'll continue to engage with the customers around this. There's submissions due on the 12th of March. No doubt the QRC, on behalf of the customers and customers individually will make their submissions on that, and we'll see where we get to. We would certainly hope that they'd recognize the flaws in the QCA decision and come back with a response that is reflective of the risk that we take as a business and the value that we provide.

Anthony Moulder - *CLSA Limited, Research Division - Analyst*

Yes. I guess -- no, no, that sounds particularly appealing. Moving on, if I could, to the transformation program. Obviously, now targeting $390 million. But obviously, this includes the reduction from the losses of Intermodal. I guess, my point on that is that they wouldn't have been a factor when this program was first set up. Does that suggest that transformation savings within the business is still -- are now getting harder to be delivered?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Pam, I might get you to answer that.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Yes. So we -- I've talked about this last year. The transformation savings would have included savings and improvements in Intermodal. But once you remove the losses from Intermodal, the opportunity to make transformation reduces. So hence, we were quite clear in saying, of the $380 million, that would include removal of losses in the Interstate business.

Anthony Moulder - *CLSA Limited, Research Division - Analyst*

Sorry, I guess we just didn't have that quantified. And today we see the quantification of that $48 million.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

I mentioned the $57 million. And once we recut the segments, it became $48 million following the recut. I mentioned $57 million last year.

Operator

Your next question comes from Ian Myles from Macquarie.

Ian Myles - *Macquarie Research - Analyst*

A couple of quick questions, please. Firstly, on the 20 million tonne impact, can you give us a breakdown of which corridors? Because I presume it's a bottom-up calculation.

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So Ian, it's an estimate at this moment in time. What you need to understand is that our modeling is not set up to even contemplate a change in maintenance practices as suggested by the QCA. We're all about modeling maintenance to improve the actual volumetric inputs -- output of the actual business. So it is an estimate of what we're currently doing, and it's not being built because their modeling doesn't give us that opportunity in a sensible time frame to do it from a bottom-up basis.

Ian Myles - *Macquarie Research - Analyst*

Okay. In terms of -- you mentioned the word flexibility in the new coal contract. Can you articulate a little bit more what that flexibility means and what risk transfers may be occurring from what used to be called new form contracts to what are probably the new version of a new form contract?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Okay, I'll get Ed to talk through that.

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Listening to our customers lately, they're really -- we've learned that they've focused an interest on 3 things. They're interested in rate, they're interested in flexibility and they're interested in performance. So we -- they're all levers we pull to win these contracts. So it's not a zero-sum game. When we talk about flexibility, the miners -- the producers look for everything from multiple load out flexibility for our trains, to nomination and ramp-up or ramp-down flexibilities depending on where their coal might be flowing and what corridor. In some cases, our customers, by tuning our commercial solution to them, they're prepared to pay more, in fact, from a rate perspective to get that flexibility. So that's what we mean.

Ian Myles - *Macquarie Research - Analyst*

But are we seeing a shift in that risk that -- like if these -- for these new form contracts or the new contracts you got, if the volumes aren't quite as much as they anticipate? Historically, you've got sort of the 10 million tonnes paid effectively for all the equipment and the like. Is that changing where you're taking a little bit more of that volume risk so it doesn't quite turn out, you're taking more risk than probably in the past sets of contract renewals?

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Not discernibly, Ian, no.

Ian Myles - *Macquarie Research - Analyst*

Okay, one final question. Just -- you talked about the Bulk and your single contract, which is really horrible and it's onerous. Why haven't you actually drawn up an onerous contract provision against that and just sterilize the impact now given you've got no intention to renew it?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

I mentioned that last year, Ian. We've provided for onerous contracts in line with accounting standards where we need to. So there's nothing further that we can provide.

Operator

Your next question comes from Paul Johnston from RBC Capital Markets.

Paul A. Johnston - *RBC Capital Markets, LLC, Research Division - Analyst*

Just a few questions from me. Just firstly back on Network. Can you just talk through, in a bit more detail, your expectations around process? You've talked about 12 March in terms of when your submission or submissions are due. What are your expectations around timing of a final decision thereafter and maybe a subsequent appeal of that decision? Can you talk through that, please?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Yes. Look, I'll get Michael to run through that process.

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

Yes, thanks. I think, yes, 12th of March is submissions. We would expect the final decision consistent with past sort of practice if we leave aside UT4, hopefully, probably towards the end of calendar '18, I think. And once we receive that final decision, we'll assess it, consider our options at that point in time. But certainly, all options will be fully assessed.

Paul A. Johnston - *RBC Capital Markets, LLC, Research Division - Analyst*

Okay. And then from a transitional tariff perspective, I therefore presume there will be another year of transitional tariffs.

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

We'd expect at least another 0.5 year of transitional tariffs through to 31 December 2018 and then obviously true-up to the final decision in the normal process.

Paul A. Johnston - *RBC Capital Markets, LLC, Research Division - Analyst*

Okay. And maybe one for you, Pam. Just on your comments on Network and the balance sheet there. In the event the draft -- sorry, the final was similar to the draft, is the view that the rating would still be investment-grade for Network? High BBB, flat or equivalent?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Our preference will be to have an investment-grade credit rating and actually to stay where we are. But again, we'd have to assess the impact of the decision to see if we can support the credit metrics.

Paul A. Johnston - *RBC Capital Markets, LLC, Research Division - Analyst*

Right, okay. And maybe just back on the Above Rail on the Coal side. Can you talk through whether you're seeing any additional opportunities in addition to the 20-odd million tonnes that you've secured in new contracts, which is obviously great news? But what else can you see out there in terms of sort of meaningful opportunities in Coal?

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

There's a few opportunities at the moment. We've got -- certainly, certainly, we're seeing the high commodity price environment bringing investors back into the market and growth plans -- organic and, in the case there, too, inorganic, the greenfield ones. We've got about 3 business development cases underway at the moment. There is one particular larger, larger producer in the Goonyella system, which is a new greenfield. It will come online around 2020. And another major contract up for tender in coming -- really later this year will be the Bengalla contract.

Operator

Your next question comes from Rob Koh from Morgan Stanley.

Robert Koh - *Morgan Stanley, Research Division - VP*

Just 2 questions on Network and then one question on WICET for me, if that's okay. Just wanting to drill a little deeper on the debt cost allowance within the regulated WACC and maybe get some commentary on how that compares to your actual cost. And then should there be a credit rating downgrade, does that mean that your actual debt costs go up further?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Okay, I might hand that question to Pam.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Yes. So it's about 50 basis points difference between the debt cost and the current proposal. Sorry, I didn't catch the second part of your question.

Robert Koh - *Morgan Stanley, Research Division - VP*

Yes. So you're saying that your actual debt costs are about 50 bps higher than the allowance? Is that what you...

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Correct.

Robert Koh - *Morgan Stanley, Research Division - VP*

Yes, okay. And then if you do get a credit downgrade as a result of the final decision, then -- do your debt costs increase further, like maybe if your rating is [creating] a debt facility?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

If the credit rating drops naturally, there's probably an increase. But again, it depends on the nature of debt because we both have debt capital markets and bank debt, and it's generally the bank debt increment which would have an increase certainly when we come to refinance and the new credit rating that is in place at that point in time.

Robert Koh - *Morgan Stanley, Research Division - VP*

Okay. All right. Yes. And then, yes, just a question on WICET. I note that the company has commented that it's still early days on that. Could we get a sense of perhaps how such a project might be funded?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Pam, I'll let you talk about that.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Yes, it's not something that we've talked about at length at this stage just because it's so early in the project. Very complex, we're not close And also It's something we'll consider at that point in time.

Operator

Your next question comes from Paul Butler from Credit Suisse.

Paul Butler - *Crédit Suisse AG, Research Division - Director*

If I can just ask a couple of questions about UT5. What response do you expect from the QCA and customers from the actions you're taking with moving your maintenance practices in line with the Draft Decision?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Okay. Well, Paul, I mean, first of all, we're aligning ourselves to what the QCA has decided is the right way to do it. So I would expect them to be terribly happy with what we're doing, although it may point out that they're profoundly mistaken in practice. From a customer point of view, I would not think that -- having been a miner and a miner of coal, I would not think our customers would particularly happy with the QCA's decision. And that's the 2 responses that I would expect.

Paul Butler - *Crédit Suisse AG, Research Division - Director*

Right. I mean, from taking this action, you're obviously protecting yourself in terms of the margin you can get, based -- given what the QCA is offering you. But -- so how much of this action is about protecting the profitability of the business as much as you can, as opposed to trying to get some change in outcome somewhere down the road?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Paul, hope -- it's a great question. And look, hopefully, my earlier explanation would point to the fact that there is very little change between a Draft Decision and a final decision based on a whole bunch of decisions and the analysis beforehand. Indeed, if you want to look and read the current Draft Decision, you'll notice a pattern where Aurizon makes a submission or the QCA comments like, "Aurizon has made a submission on this item. Our consultants have made a submission on this item. We go with our consultants." They, not invariably, but they mostly ignore what we say. So I suspect that we'll -- that they will just continue to march on in their current form. That's all the data I actually have, and it's the rationale for acting in the way that we've acted because -- and it's because of that retrospectivity, I'm already 8 or so months in to a year where I've been whacked with this decision which I can't even find a sensible basis for it, and I have to adjust because the process is broken.

Paul Butler - *Crédit Suisse AG, Research Division - Director*

Yes. So if we look further down the road to what happens with UT6 or the future of how this asset gets regulated, I mean, what hope do we have that there will be a different approach then than there has been now?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So look, it is very hard, given it's hard to see through the UT5 decision other than to base it on whatever happen in the Draft Decision is likely to be pretty close to the final decision. The UT6 and UT7 will -- going on, will always depend on the parties getting together and deciding whether they continue to fundamentally support the process that we're going through at this moment in time, and the result -- and the way it results for industry. The end of day, there's a bunch of factors. I think it's 7 factors that the QCA must take into account when it's out making its decisions. And they've got to demonstrate that they've actually taken those into account at some point to someone, one of which is the efficient operation of the rail servicing the coal industry, so it's part of the supply chain. Other impact factors -- I won't go through all of them, it would bore you silly -- but another impact is actually the successful operation of our business. So we are meant to actually conduct business and be rewarded for it. So none of that appears apparent in the current decision. And at some point in time, that's where the regulation points to the quality of the decision -- on balanced decision that they're meant to make. And there was various review processes in lengthier cycles that look at how regulators perform.

Paul Butler - *Crédit Suisse AG, Research Division - Director*

If I can ask, I mean, clearly, customers are going to be frustrated with this and there's likely to be a public perception government backlash. How do you manage the risk that Aurizon gets blamed for more of this?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So at the end of the day, we are following a decision by a regulator, okay? This is not Aurizon waking up one morning and deciding to do a whole bunch of things. We've got a regulated decision, and it requires us to make these changes. We acknowledge that the changes are not sensible, and we wouldn't do them. But we're being driven that way financially by the regulator to do that. It is not Aurizon's job to subsidize the coal industry in Queensland. It's our job to be a very good supplier of rail services and satisfy our customers within a certain series -- boundaries of constraints and that sort of stuff, and we work very hard at doing that. As I said, December was our highest customer satisfaction score. We thought we were on a good path, and then we got side swiped, yes. And it was also record volumes in December, which I would have thought it would be fundamentally exciting to both the above rail operators and the coal miners themselves.

Paul Butler - *Crédit Suisse AG, Research Division - Director*

Okay. And just one last one, the cost savings that you're on target to achieve of $380 million, how much of those are going to come from the network business as opposed the above rail?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

That $380 million excludes savings in the Network businesses, just the Bulk and Above Rail coal business.

Paul Butler - *Crédit Suisse AG, Research Division - Director*

Okay. So you had, I think, $20 million of transformation benefit in Network in the half?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

It's not included in the number of $42 million.

Paul Butler - *Crédit Suisse AG, Research Division - Director*

But what would have the savings been -- I can't recall what the savings you sort of recorded in the Network business over the sort of same period where you've been going after this $380 million.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

There was an element of the true-up that I mentioned when I went through. So there was the UT4 previous corporate cost true-up through the UT4 decision. But there's also generally, and we'll continue -- even if the Network numbers are not included in the transformation, we'll continue to drive improvement in costs in the network, so that's just part of the normal process.

Operator

Your next question comes from Scott Ryall from Rimor Equity Research.

Scott Ryall

I have a few questions. On the Coal division first. You've got volumes up 4%, revenue up 4%, operating costs up 5%, so just leaving aside the gains made from slightly lower depreciation expense, could you just comment on why you're seeing a lack of earnings leverage from all the transformation work that's been going on? And maybe with that, just explain a little bit more about these costs supporting volume growth. Are they upfront costs that then peter away a little bit because you're implementing contracts and things like that?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Ed, I'll get you to answer that. Thanks.

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Yes. Thank you, Andrew. Yes, you nailed it. I mean, essentially, a large part of the -- why the revenues aren't flowing through to the volume, revenues aren't flowing through the EBIT line, is largely the preparation for these 2 new greenfield contracts coming online. So in the case of the Byerwen contract, we've been readying fleet. We've quite the short-dated ramp-up, and so we've been incurring those costs and ensure we're there for the customer when they want to start railing. Similarly, because of the preloading in terms of training of drivers for our MACH contract, we're bringing the 20 million tonnes volume on, in the ramp-up. You've got to be hiring people several months up to a year in advance of when the volumes hit.

Scott Ryall

Okay. Would you be able to quantify what you think the impact of, I guess, investing ahead of contracts are? Just to get an idea of the earnings leverage that you are delivering in your underlying business?

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Probably not really, Scott. It's commercially sensitive.

Scott Ryall

Okay, no problem. All right. Can I just switch to Bulk, then? Bulk, obviously, the EBIT has changed quite a bit, but EBITDA was still down in line with your revenue or costs were still down in line with the revenue. So you haven't made what I would call significant EBITDA turnarounds. And as Pam discussed, most of the changes in EBIT were due to depreciation reductions due to impairment. So in terms of the changes that you've talked about, Andrew, with your 3 contracts moving towards retained, when do we actually start to see the benefits? Will that come through from the second half? And I mean benefits in terms of cash flow as opposed to EBIT.

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Yes. Absolutely fair question. I will get Clay to talk through that.

Clay McDonald - *Aurizon Holdings Limited - Group Executive of Bulk*

Last year, we spoke about a Bulk turnaround plan that would take 3 years to implement. We also said there was no easy answers in that turnaround plan, that it would take a dedicated Bulk team focusing each day on trains, each day on depots [and our] customers. So the 4 things we said we'd focus on with the re-contracting of legacy contracts. And both those that have come up in the period that have been awarded, have been awarded to us. So Cement Australia and the hook-and-pull work trains for QR. The second thing we said was lower cost base. You could probably see in the numbers there, our FTE numbers are down 195 or 16%, not just on the Mount Isa closure, but through the Western business. We're now moving to driver only, and the maintenance being more productive over there. So down 16% or 195. Also see labor productivity up 3% in a comparable period. The other thing we talked about was improved customer service, was the third area we'd focus on. And pleased to say seeing some early progress of dedicated bulk management on our particular customer base. So good example, 420 trains run for our customer, IPL, on the Mount Isa line without failure. So that's -- we haven't had a failure in that service since September last year. Also, improved on-time performance to KAL Freighter since the introduction of the new infrastructure over in Kwinana. Finally, growth on the revenue line. This is hard. It's hard going. There is growth opportunity there. We see tonnage opportunities in the Western province, the Western Queensland province, moving from somewhere around 4.9 million tonnes to 6.2 million tonnes in the next couple of years, so we'll be chasing those. And also, over in WA. But I guess, the one growth piece of business we brought on line, MMG, starting as per plan in November this year.

Scott Ryall

All right, and then maybe I can move to...

Clay McDonald - *Aurizon Holdings Limited - Group Executive of Bulk*

(inaudible) so I thought I'll take every opportunity I could.

Scott Ryall

Yes. No, no. On UT5, could you, Andrew or maybe Michael, could you just confirm post the ruling, which was pretty close to Christmas, I imagine -- I'm pretty sure your head office is closed and I imagine a lot of other head offices are closed. What one-on-one engagement activity were you able to do prior to 2 weeks ago? I think you mentioned the -- when you changed your practices?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Yes, I'll get Michael to run through all that.

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

Yes. So before Christmas, a couple of days after the decision, I did meet with Charles Millsteed, the CEO of the QCA. So had a long discussion with him about the decision and the process going forward. In terms of the customers, we speak to our customers every day, talk to them about the impacts, and we've also had discussions with the QRC. I think, at the moment, we'll continue to engage with them and try to come to bring them to an understanding of the issues associated with the decision, both around maintenance practices and overall risk and the impacts on the supply chain as a consequence.

Scott Ryall

Okay. So they wouldn't have been surprised by your -- what looks like a group email on the 30th of January that would have heard most of your discussions -- would have been done one-on-one with your 20-odd customers prior to then?

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

I think certainly not with all of them. I think they shouldn't have been surprised. They saw the decision and understood what the implications were and what the QCA was advocating. So -- and I understand the retrospectivity of it. So I don't think they should have been surprised by it. And in terms of detailed discussions. I mean, we spent a lot of January working through what the impact of the decision was, how we needed to respond to it, as you can appreciate. You can't change maintenance practices overnight, there's a strong safety element to them, and we needed to give careful consideration to that. So we didn't give detail to the customers on a -- in significant advance of the decision we made on the 30th of January, nor will we in relation to further changes we have to make. We need to make them now, as Andrew said, and we'll be making them as soon as we can.

Scott Ryall

Okay. So if I then step back to customers because, ultimately, prior to 12 March, your -- I guess one of the hopes you have is that customers are following behind your position. Would that be a fair comment?

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

Yes. We'd always hope that customers recognize the value we're providing and that the amount we're seeking is a reasonable reflection of that value and the risks we're taking. So absolutely, we'd be hoping that.

Scott Ryall

So most of the submissions last year, let's say, from customers, I mean if I use the Rio one because that's a business close to Andrew's heart, where Rio identified that -- and specified some quite specific improvements through their own labor productivity, rail maintenance unit costs improvement in overall operations office that were quite substantial and talked about in line with much of the resources sector. And then the last line is the modest productivity gains and cost-plus approach to capacity management employed by Aurizon Network were under closer scrutiny. How -- I mean, that's obviously 9 months ago now when they submitted that. But how do you change the customer perception that you guys just haven't cut your costs in line with the resources sector?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So I mean, it is a great question. And the reality is, it takes time. Even after you've started the process of reducing costs dramatically, it takes time for people to actually notice that. When I started -- I inherited -- when I started in this business, the first thing I was told was the network is gold-plated by just about everybody. I've seen parts of the network that are nearly as old as I am, and that actually are being -- shepherd through at an absolutely minimum cost. So the reality is, all businesses can improve. But when an organization gets a sort of reputation it had when it was in government days, I can understand that, that takes quite a bit of time to unwind. Customer satisfaction scores don't change overnight. You've got to regularly and reliably actually work to improve them. So the reality is that's quite a substantial amount of effort that's required to do that as from a customer management point of view. At the end of the day, this is a regulated process, and the regulator makes the call and actually has shown little regard to the submissions that are being made compared to its own internal decision-making.

Scott Ryall

Okay. And I guess, ultimately, will -- do you think customers will think your -- if I just do a very quick math. You make $2 million of EBIT for each tonne that you haul. Obviously, there's some specifics around that. But are customers really going to think that you're credible in terms of putting your own volume growth at risk? I mean -- is that something you expect them to believe?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

So go back to the original issue that we have with the QCA which is, they're asking us to actually undertake maintenance in a way that will massively impact volume. We don't want to do that and we don't want a price that's actually set as if we are massively impacting volume, but then subsidize the volume. The -- and the second thing is just look at the weighted average cost of capital outcomes for regulated businesses across Australia and imagine: Is a water authority supplying water to domestic consumption in Brisbane a riskier undertaking than working in a tropically cyclone-impacted coal industry in Queensland? And the answer is obviously not. So those are the things that we have profound challenges with. And we will work as hard as we can to convince people that this is -- this shouldn't -- the decision should not stand. But at the end of day, if you look at the process of the history of the QCA and actually action, they don't change for anyone.

Scott Ryall

Yes. Sorry, you won't get an argument with me on the WACC one. But in terms of -- in the event that you are unable to change the WACC, as you'd said, which is minimal change between draft and final decisions. When do you start thinking about structural options to get the network in the hands of investors who may actually have that cost of capital as opposed to what tends to be a slightly higher cost of capital in the public market?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Now I understand where you're going. Sorry, it must be too early in the day or something. We'll have a look at how the process plays out with the current issues with the -- between a draft decision and a final decision. The sort of options that you're talking about is something we haven't yet contemplated. Always remains an option that could sit out there, but currently not part of our thinking.

Operator

Your next question comes from Guy Bunce from JPMorgan.

Guy X. Bunce - *JP Morgan Chase & Co, Research Division - Analyst*

Andrew, in the event the QCA's final decision is similar to its draft, are there any precedents we should think about where QCA's decisions have been overturned in the past?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

I might handle that straight to Michael.

Michael Robert Riches - *Aurizon Holdings Limited - Group Executive of Network*

Thanks, Guy. I don't believe there's been a judicial review process that has been successfully undertaken against the QCA or undertaken at all to date. But that's not going to deter us if that is the right option to take based on the final decision.

Guy X. Bunce - *JP Morgan Chase & Co, Research Division - Analyst*

Okay. My next question is just around the potential impact of Cliff's early termination. It's my understanding that, under that contract, Aurizon is probably generating revenues each year of around $100 million to $150 million. And yet, according to the management team of Cliff on their recent trading call, they're suggesting that the contingent liability for both the rail and port operator is only around $80 million. So are you able to talk about the potential impact of that early termination?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Not at this stage, given that the termination amount changes depending on when they actually terminate the contract. So we need to have the conversation and understand what their plans are to be able to put a figure on that.

Guy X. Bunce - *JP Morgan Chase & Co, Research Division - Analyst*

So they've indicated most likely the end of this calendar year. Are you able to, with that sort of information, Pam, give us a number?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Yes, we've been in contact with the Cliff's management, and they have advised us they will be in a position probably around the end of February to advise of what their mine plan is and any ramp down or closure of that operation.

Guy X. Bunce - *JP Morgan Chase & Co, Research Division - Analyst*

Okay. Final question. Just you talked about the pressures that you're seeing in terms of coal contract prices. Can you provide a bit of quantification around that?

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

That's commercially sensitive. But I can certainly say we're happy with the returns we've been getting. In the case MACH and Byerwen, I mean, proud to win the business in what's a very competitive market at the moment. There's no doubt that competition is putting downward pressure on rates in a historical conference -- context, but we continue to find ways to leverage asset productivity and synergies. An example of that is the MACH contract where we -- because we won the AGL and we set up a depot near Muswellbrook, we're able to then service MACH which is immediately next door, so we don't have the additional -- we've got economies of scale there, we've got the dedicated maintenance and on-train repair at Hexham, which is a new technology. And then we can -- we have been able to move quickly to deploy locomotives and people from Intermodal to avoid some of the ramp-up costs in that particular contract. So transformation agenda is the -- transformation is the key, ongoing asset productivity. The DP train fleet where we're installing first mover in the Hunter Valley, and in cab technology. So we're still able to find a way to strike deals that work for -- as a win-win with us and the customers.

Guy X. Bunce - *JP Morgan Chase & Co, Research Division - Analyst*

Can I just be a bit more direct, then? Are they margin-accretive contracts that you're winning here or margin dilutive?

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

That is too direct. We are -- we're growing volume and we're growing value.

Operator

Your next question comes from Owen Birrell from Goldman Sachs.

Owen Birrell - *Goldman Sachs Group Inc., Research Division - Metals and Mining Company Analyst*

I'm going to try and keep my questions fairly short. Just on Above Rail coal, just in terms of the sort of the 20 million tonne reduction in output that you think will start to flow through the network. Just running around the service requirements you have within your contracted customer base, can that accommodate that sort of 10% fall off in volumes without you having to specifically take any hits to those contracts. And just in terms of the new sort of flexible contracts that you've been signing, just wanted to confirm that the 70% take-or-pay structure still holds. And can you give us a sense of what the headline rates have changed by into these new contracts?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Yes, look, I'll answer the first part of that which is the 20 million tonnes is a estimate in global for the entire network. And Ed simply doesn't -- isn't allowed to see the detail -- what detail there is behind that calculation. Do you want to talk about the take-or-pay thing?

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Yes, there was -- sorry, could you just sort of repeat the last 2 questions?

Owen Birrell - *Goldman Sachs Group Inc., Research Division - Metals and Mining Company Analyst*

Yes, just around the new contracts that you've signed. You were talking about them being more flexible. Just wondering whether the take-or-pay, the 70% take-or-pay structure, still holds with -- consistent with the new form contracts previously. And you've indicated that the rates have become more competitive. I'm just wondering if you can give us a sense on what the decline in the headline contract pricing has been.

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Yes. So in terms of -- just in terms of new form contracts, both of the contracts are new form contracts and both have take-or-pay and [RA] capacity charge provisions in them. So I won't talk to the exact -- the exact [provisions] because that does change depending on the customer. But on balance, we're maintaining the same proportion of fixed income across our portfolio. The -- in terms of rates, we're talking about -- I can't -- I won't go into the scale of that, but it's incremental. It's -- and largely, as I said on the previous question, we're -- we've been able to maintain our value or grow it based on continuing to transform our operations.

Owen Birrell - *Goldman Sachs Group Inc., Research Division - Metals and Mining Company Analyst*

Okay. And just -- I've got a couple of just follow-up questions for, I think, probably for Pam. Just wondering on Intermodal, you mentioned that you've taken a $40 million deposit on the sale of the Queensland Intermodal assets. If the ACCC rejects that transaction and you're forced to close those assets, is that deposit refundable or what proportion of that deposit is refundable? And can you, on the Network side of things, have you got any, I guess, early guidance on the likely true-ups and make-goods for the Network business in FY '19? Have we got a bit of a run rate on that so far?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

So to your first question, a small proportion is not refundable, without getting into the specifics. And sorry, the second question, the true-ups with Network?

Owen Birrell - *Goldman Sachs Group Inc., Research Division - Metals and Mining Company Analyst*

Yes. Just into 2019, whether we've got any sort of visibility on that yet.

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

No. I think it obviously depends on the outcome from the UT5. So if we have transitional tariffs for the rest of this year, obviously, there's a wash-up from this year to the final decision, and that will then hit the forward years from FY '19 through to '21. So usually -- I mean, if you look at past process with the QCA, they would have washed up any difference in the remaining years rather than the current year that's in play. And the only other wash-up that you're likely to see is any sort of -- if you know that there's already a 2-year lag with revenue cap, so if there's a revenue cap that would drop into that year, so FY '17 into FY '19.

Owen Birrell - *Goldman Sachs Group Inc., Research Division - Metals and Mining Company Analyst*

And what's that sitting at the moment? Do you have a sense on that?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

That was the almost $40 million. I think that's $39 million. If you remember, we had Cyclone Debbie, so we have a shortfall in our revenue in FY '17. So the upside goes into FY '19.

Owen Birrell - *Goldman Sachs Group Inc., Research Division - Metals and Mining Company Analyst*

And about $39 million a year?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Yes.

Operator

Your next question comes from Nathan Lead from Morgans Financial.

Nathan Lead - *Morgans Financial Limited, Research Division - Senior Analyst*

Most of my questions have been taken. But if I can just ask just a couple. Just first on Slide 51. Just the maturities in those early years, FY '20, '21, '22, can you give us a bit of color about whether there's any mines in there that are likely to draw towards end-of-mine life or contracts where you know a competitor has already grabbed that volume?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Nathan, we're just finding Slide 51. Just hold on a second.

Nathan Lead - *Morgans Financial Limited, Research Division - Senior Analyst*

Yes. The coal haulage contract.

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Coal haulage contract. Sorry.

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

Sorry, Nathan. I was flicking, too. Could you just restate the question please?

Nathan Lead - *Morgans Financial Limited, Research Division - Senior Analyst*

Just in those early years, FY '20, '21 and '22, are there any mines within those contracts there that are going to be towards end-of-mine life and then expire? Or is there any contracts there that have already gone to a competitor or either been -- there's been a competitive process already run and a competitor has grabbed them?

Ed McKeiver - *Aurizon Holdings Limited - Group Executive of Coal*

I'll take the last question first, and the answer to that is no. There's none of those contracts that have gone to competitors. And secondly, in relation to -- I'm looking through -- flicking through the detailed list I have here. I mean, in relation to the end-of-mine life, nothing substantial largely in the FY '20, '21, '22 period. All of those mines, probably with the exception of New Acland's mine in the Southwest corridor, which is still awaiting a judicial review in March. And so there's a brief -- our contract, that as most -- commentators and analysts know, that mine will depend on the approval processes other than that.

Nathan Lead - *Morgans Financial Limited, Research Division - Senior Analyst*

Yes, okay. Just maybe one for Pam, just a bit of detail. I mean, often, there's been a chat about will Network -- will there be a sale of it, will there be a sort of sale to minority or a spin-out or something. Can you just talk through the capital gains tax consequences of that? Because my understanding was that Aurizon effectively have bought that lease from the government for $1, so there's quite low capital gains tax base. If you could sort of run us through that?

Pam Bains - *Aurizon Holdings Limited - CFO & Group Executive of Strategy*

Nathan, it's not something that we've considered. So I haven't sat and thought through the tax impacts.

Operator

There is a follow-up question from Scott Ryall from Rimor Equity Research.

Scott Ryall

Sorry, Andrew. You mentioned WICET, I was wondering if you could talk -- I know discussions are ongoing, but what are the milestones you're looking at over the course of this calendar year in terms of progressing that transaction, please?

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Yes. Scott, rather than actually get into a milestone discussion, I think the biggest single issue with WICET is the debt challenge that they're publicly noted for actually having and how they actually deal with that. And I understand it's probably better to talk to them to get accurate information on when those big issues fall due with how they actually handle their debt. But that would -- those sort of decision-making points would set milestones. But I don't get to sit on their board, so I don't actually -- or speak publicly for them, so I probably shouldn't get into much around the milestones there except that, that's one of the -- that would be a key factor in the progress of that deal.

Operator

There are no further questions at this time. I will now hand it back for closing remarks.

Andrew T. Harding - *Aurizon Holdings Limited - MD, CEO & Director*

Well, look. Thank you very much, everyone, for what has been, so far, the longest results presentation that I've done, and we've covered quite a few topics. I do hope that, while most of the questioning was on more of the strategic issues, that you do note the -- how solid our results were and the improvement in the underlying business, which is key to us being successful as we go forward. So thank you very much, everyone. Look forward to seeing you at a later point in time. Thank you.

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