

## **APA Group Annual Meeting 2010**

### **Chairman's address**

Ladies and gentlemen,

This year APA Group celebrated 10 years of operations since listing on the ASX in June 2000, and during its short history has continued to deliver value to its securityholders each year. In the 2010 financial year, APA has delivered another strong financial performance and continued to enhance its asset portfolio and energy businesses.

Our success is not just due to the nature of our business that we have built over the last 10 years, but also how we operate and manage the business and how we are developing energy opportunities.

We have gas infrastructure assets transporting natural gas right across the country. APA transports more than half the gas used in Australia, in a market where both supply and demand are increasing.

Much of our revenue streams are secured by long- term contracts and the regulatory regimes in which we operate.

And we have the internal skills, experience and knowledge to manage and operate our assets and investments and develop the many profitable opportunities that still lie before us.

In 2010, APA maintained its reliable performance in the midst of challenging market conditions. We continued our strategy of growing the business sustainably and profitably and strengthening our financial capability. As a result, APA is now in a stronger position to continue its steady growth in a rapidly changing and highly competitive energy environment.

#### **Financial performance**

The financial result for 2010 was driven by the continued strong performance and growth of our gas transportation and distribution business, and continues the positive trend in all key financial measures. Over our ten year history, we have delivered consistent financial results that reflect our secure and growing business.

Since listing more than decade ago, total returns to APA securityholders have exceeded the broader market and our peers, with a total return to securityholders averaging 16% per annum.

In other words, one dollar invested in APA at the time of listing is worth in excess of four dollars today, and is more than double the value of a dollar deposited in the bank or an investment indexed to the All Ordinaries. I trust that you will agree with me that this is a good performance from a largely regulated infrastructure business.

The reason for this performance is evident in our results for 2010.

APA continues to be a strong and secure cash generating business, achieving a 14.6% increase in operating cash flow to \$268 million.

Despite the loss of earnings from assets sold to Energy Infrastructure Investments in the 2009 financial year, earnings before interest, tax, depreciation and amortisation (EBITDA) has increased by 3.5% to \$460 million.

After adjusting for the contribution of these divested assets, the EBITDA of APA's current business increased by 8.7%.

The increased performance was driven by the growth of the gas transmission and distribution business, principally in the sale of additional capacity from recent pipeline expansions.

The increase in operating cash flow provided the basis for increased distributions to securityholders.

On the 25<sup>th</sup> August, the board declared a final distribution of 17 cents per security, taking the total distribution for the 2010 financial year to 32.75 cents. This is a 5.6% increase on the previous year, and represents APA's tenth consecutive year of maintaining or increasing distributions.

As we have done since the listing of APA, we have continued to ensure our distributions are fully covered by operating cash flow.

### **Capital management**

Funding for APA's growth projects during the year was sourced primarily from cash remaining in the business after payment of distributions to securityholders along with \$142 million of new capital raised through the Distribution Reinvestment Plan and the Security Purchase Plan.

Throughout the year, we maintained our focus on further strengthening our balance sheet. We have credit ratings from each of Standard and Poors' and Moody's, confirming APA's investment grade status. With these ratings in hand, we continue to focus on our forward refinancing obligations, actively implementing a capital management strategy that is designed to extend the term of our debt in line with the life of our long term contracts for transportation and our asset portfolio, whilst at the same time minimising future interest costs and diversifying the sources of our longer term funding.

This strategy was recently endorsed by the strong interest and attractive pricing achieved for the 10 year \$300 million of Australian dollar bonds that we issued in July 2010. This issue was the first by a BBB/Baa2 rated corporate in Australia and was described by market commentators as both "historic" and "ground breaking".

I've received a number of questions from securityholders relating to our level of debt and whether it is appropriate for APA.

Infrastructure businesses like APA typically carry a high level of debt given the capital intensive nature of the business and the long-term certainty of revenues.

At APA we are comfortable with the level of debt that we carry for a number of reasons:

First, APA's business generates sufficient cash to more than cover the cost of debt. After meeting our interest costs we generally have in excess of \$200 million in free cash that we then use to pay distributions to security holders and to help grow the business by reinvesting back into the business.

Second, we closely control the level of debt that we carry relative to our assets, our equity and the cash flow we earn each year. The aim is always to maximise returns to APA securityholders in a prudent and sustainable manner.

Third, we have committed to retaining our investment grade credit ratings. These ratings benefit APA in allowing the company to access a broader range of global credit markets.

Finally, the longer term nature of our assets and revenue contracts give us a high level of confidence that we can operate with the current levels of debt in the longer term. We maintain very robust forward looking forecasts of our revenues and costs to ensure that this remains the case. We also look to ensure that our debt matures over a long period of time - currently from 2011 out to 2022 - so that we never have too much debt to refinance or repay at any given point in time.

Another question concerned rising debt costs. We, like all companies, have seen debt costs increase, particularly as a result of what has been generally referred to as the Global Financial Crisis.

However, we manage our debt prudently, insulating the business from interest rate shocks by hedging a large portion of our debt. Consequently the business has experienced only a gradual rise in debt costs.

Another impact of the Global Financial Crisis was a general limiting of access to debt facilities across the globe. As a precautionary measure during this time, APA increased its debt headroom; that is, ensuring we had access to a greater level of undrawn debt facilities. With what looks like improving credit conditions ahead of us, we are looking to take a prudent approach to decreasing the amount of this headroom over time.

We will continue to manage the balance sheet prudently, maintaining our debt and equity in a manner that will preserve APA's investment grade credit ratings, and at all times looking at strategies to minimise the impact of debt costs on the business.

### **Strategic achievements**

Through the year we adhered to our strategy of growing the business sustainably and profitably. We continue to actively expand the capacity of our infrastructure to meet the growing demand for natural gas, this year investing in more than \$200 million of organic growth projects. Most of the focus has been on the east coast of the country, expanding our New South Wales, Victorian and Queensland gas pipelines and distribution systems. The ongoing prospect of growth of our network remains an exciting challenge for APA and Mick McCormack will provide more detail on how we are doing this in his address.

An acquisition we made last year was focused on enhancing our infrastructure. We acquired the newly built Berwyndale to Wallumbilla Pipeline in Queensland, at a price not much more than construction cost, together with a long term gas transportation agreement. This pipeline connects our Roma to Brisbane pipeline to the Surat Basin in Queensland and ensures that gas coming from the Coal Seam Gas fields of that state is connected to our network of pipelines.

During the year, we also acquired a 17% interest in Hastings Diversified Utilities Fund, the assets of which include pipelines that connect with APA's pipelines. We've taken this position in support of the expansion of Hastings' South West Queensland pipeline, which delivers gas into

the Moomba Sydney Pipeline – the Moomba Sydney Pipeline represents almost one quarter of APA’s business.

### **Board and management**

Although not unexpected, George Ratilal resigned his position as a director in August this year, after serving on the APA board for approximately 3 years. George holds the position of Executive Vice President Finance of Petronas, and has been a valuable contributor to the APA board over that time. However, he was recently promoted to Executive Director of Petronas – sitting on that company’s main board - and after considering his additional commitments that appointment entails for him, George decided to resign from the APA board.

I would like to take this opportunity to acknowledge George’s valuable contribution to the board, and am very pleased that we will retain our contact with him in his role as alternate director for Muri Muhammad, Petronas’ appointee on our board.

An important responsibility I have as your Chairman is to ensure that APA’s board and management has the requisite skills, experience and motivation to deliver the objective of maximising value to securityholders.

I am pleased that APA has both a strong Board and management team that have been key components of producing consistently solid financial results.

Having regard to recently announced changes to the Corporate Governance Principles and Recommendations issued by the ASX Corporate Governance Council, as well as George Ratilal’s resignation, the board will continue to review the size, skills and composition of the board.

### **Outlook**

Looking ahead, the Board remains focused on ensuring APA delivers secure and growing operating cash flow from all parts of our business.

Our strategy remains consistent. The demand for natural gas continues to increase, and consequently the demand for our transportation, distribution and storage services is also increasing. APA will continue to benefit from asset expansion and a broad range of services underpinned by contractual and regulatory arrangements.

In the first quarter of this financial year, the business is performing in line with our expectations and in line with guidance we have given to the market when announcing our full year results in August.

APA’s ongoing level of distribution payments to securityholders balances the Group’s need to retain sufficient equity in the business to support the funding of its significant growth prospects whilst also increasing returns to securityholders by, on average, 5% over the medium term.

Barring unforeseen circumstances, we affirm our intention to increase distributions in the 2011 financial year by at least 5%, with distributions fully covered by operating cash flow, and to achieve earnings before interest, tax, depreciation and amortisation (EBITDA) within a range of \$465 million to \$485 million.

In conclusion, I would like to acknowledge and thank my fellow APA directors for their contribution and commitment this year.

Also, on behalf of the board, I would like to thank all APA employees, led by Mick McCormack and his management team, for their continued energy and skills that have contributed to our continued success.

Finally, I thank you, our valued and loyal securityholders, for your ongoing support of APA.

## APA Group Annual Meeting 2010

### Managing Director's address

On our 10 year anniversary I am proud to report APA has had another strong year, building on its history of solid performance.

Our success is the result of maintaining our focus on generating value for our investors, adhering to a clear strategy and adeptly responding to the challenges and opportunities of a dynamic energy industry.

As the last remaining member of the leadership team that floated this business in June 2000, I have been part of APA's growth and evolution.

From a small team of six people managing APA's assets, we have progressively built our internal expertise to become a fully integrated operating business with now more than 1,100 people.

Our strategy has been consistent since listing 10 years ago – to enhance APA's asset portfolio, focussing on gas infrastructure assets in Australia's growing gas market.

We have adhered to our strategy and expanded our portfolio from one key asset in 2000 to now having an unrivalled asset footprint of gas pipelines and distribution networks across Australia, touching every gas-producing basin and connecting to every major market.

Today we are Australia's largest gas infrastructure business – delivering more than half the gas used across the country each year, and almost three quarters of the gas used in Australia's eastern states. From Perth to Brisbane, Darwin to Melbourne, you'll find APA delivering clean natural gas that fuels our economy.

This year, we continued to increase the capacity of our pipelines and infrastructure to meet customers' demands for more services. These projects will deliver revenue certainty over the longer term, with revenue secured under long term contracts or regulatory arrangements.

We clearly expect this growth to continue into the next decade as natural gas becomes an increasing part of Australia's energy mix.

#### **Business performance**

Our Chairman spoke earlier of our strong financial result this year.

I will now talk briefly about the performance of each area of the business, as well as outline the projects and opportunities that lie ahead.

Our strong result this year was driven by the recent expansions on our pipelines.

Our largest business segment, **Gas Transmission and Distribution**, recorded an increase in EBITDA of 5%, to \$409 million - mainly due to the sale of additional capacity on the Moomba Sydney Pipeline, the Carpentaria Gas Pipeline and the Goldfields Gas Pipeline. This was offset by reduced gas volumes through the Victorian Transmission System due to warmer winter weather.

The EBITDA performance of our **Asset Management and Energy Investments** segments also contributed to the increased result, reflecting a full year operation of the Energy Infrastructure

Investment assets, the addition of our investment in Hastings Diversified Utilities Fund and our increased equity interest in Envestra.

Asset Management's EBITDA contribution was \$32 million, while Energy Investments was \$19 million.

I will now take you on a cook's tour of the Gas Transmission and Distribution business by state, providing more detail on performance in 2010 as well as the projects we have currently underway or planned for the 2011 financial year.

Starting in the eastern part of the country, we'll work our way around.

## **Queensland**

APA's three gas infrastructure assets in Queensland performed well.

Revenue from the capacity added to the Carpentaria Gas Pipeline in 2009 boosted Queensland's performance.

During the year we acquired the recently built Berwyndale to Wallumbilla Pipeline for \$87 million. This included a long term contract to deliver gas for AGL Energy. The pipeline is situated close to the Roma Brisbane Pipeline and provides both operating and revenue synergy benefits.

The Roma Brisbane Pipeline is the only pipeline delivering gas into Brisbane, and is physically interconnected with APA's Gas Network that services south east Queensland, including southern Brisbane.

We continue to grow the gas network into new housing development areas between Brisbane and the Gold Coast, this year providing almost 2,000 new home sites with access to gas.

We completed the construction of a lateral connecting the Roma Brisbane Pipeline to a large industrial customer. In 2011 we will begin further expansion of the Roma Brisbane Pipeline in line with new customer contracts.

## **New South Wales**

Our New South Wales assets performed very well this year.

We continued the expansion of the Moomba Sydney Pipeline, completing the second year of our five year incremental expansion program, and reconfiguring the operation and location of a number of compressors on the pipeline.

The increased sale of capacity on the Moomba Sydney Pipeline was the main reason for New South Wales' strong performance.

We commenced the expansion of the southern section of our New South Wales system in response to the transportation and storage requirements of gas-fired power generation in the region. This involved looping, that is duplicating, 61 km of the Young to Wagga lateral.

The additional benefit for this power station, as well as other customers on our pipelines, is the ability to source gas from more than one region, since APA's pipeline systems in New South Wales and Victoria are interconnected.

The expansion across our assets, including the looping project I just described, is being designed and managed by APA's people. We utilise our extensive internal know how not only to maintain and operate our assets, but also to design and build our assets, adding more lines to our map.

This slide on the screen shows various stages of constructing the Young to Wagga lateral. Construction activity is almost complete. It was due for completion in September, but the rain this winter has delayed completion until later next month. The pipeline is buried adjacent to the existing lateral and the land will be returned to its former condition, with only the odd pipeline marker to signify what has taken place.

### **Victoria and South Australia**

The start of the 2009 winter was unusually warm, and this affected Victoria's performance, which was down on the prior year. The colder start to the 2010 winter should mean an improvement on last year.

Nevertheless, the delivery needs of the Victorian Transmission System continue to grow, and consequently we commenced the expansion of the northern part of the system, as approved within the regulatory arrangements.

Once both expansions in Victoria and New South Wales are completed, customers in both states will benefit, as we will effectively increase our ability to move gas between the two states, adding further flexibility and improving security of supply.

### **Western Australia and Northern Territory**

The result in Western Australia and Northern Territory was solid.

The sales from the additional capacity on the Goldfields Gas Pipeline following the installation of two new compressors in 2009 provided additional revenue.

However the regulatory decision handed down by the Western Australian energy regulator, ERA, in August this year has resulted in a 10% decrease in regulatory tariffs going forward. While this regulatory decision only affects 40% of the pipeline's revenue, we are appealing the decision through the appeals process.

Our Parmelia pipeline and Mondarra gas storage facility provide flexibility to customers who transport gas to Perth and surrounding areas. Following the Varanus Island incident in 2008 and consequent interruption to gas supply to Perth, the storage facility has become a more important piece of infrastructure to ensure security of gas supply for that city.

We have commenced an expansion of the Mondarra gas storage facility with initial engineering design work and reservoir assessment activities underway. We are now working with our customers to secure contractual arrangements, and will then proceed with the expansion program to meet their longer term gas storage needs.

This is an exciting project, supported by our customers and the West Australian Government, and I look forward to reporting to you on its progress through the year.



## **Energy investments and Asset Management**

APA has minority equity interests in a number of energy assets and energy businesses across the country. These include:

- Envestra – Australia’s largest gas network business,
- the SEA Gas Pipeline,
- Energy Infrastructure Investments,
- EII2, which owns the North Brown Hill Wind Farm being developed,
- the Ethane Pipeline, and
- Hastings Diversified Utilities Fund.

We earn a healthy return on each of these investments. And by utilising our internal skills and know-how, we play an active role in managing and/or operating these assets, with the exception of Hastings. Although we don’t operate its assets, our investment in Hastings is strategic since its gas transmission pipelines connect to a number of APA’s pipelines.

### **Growth drivers**

We are delivering security and growth to our securityholders by profitably and sustainably growing the business.

We have expanded and enhanced our asset portfolio year on year. In the 2011 financial year we are progressing more than \$200 million of growth projects and opportunities, as you can see on the map. These will deliver secure revenue in the future, being either underwritten by contracts or included in regulatory arrangements.

As we look forward we see many more development opportunities for our business, and these are driven by a number of factors such as gas supply and demand increases, the growth in gas fired power generation and the need for gas storage. There are also development opportunities unique to APA as a consequence of our integrated asset portfolio and our internal asset management and operating capabilities.

I’ll focus briefly on how gas fired power generation is driving infrastructure growth.

The increasing use of gas for electricity generation is influenced by carbon reducing initiatives such as the federal government’s recently legislated Renewable Energy Targets. To meet this target, investment in wind generation is increasing. Subsequently gas-fired peaking plants will be required to provide back up electricity for when the wind doesn’t blow.

In Queensland, the government’s state Gas Scheme is encouraging the greater use of gas for electricity generation, and this has been the catalyst for significant new gas fired electricity generation in that state.

It is not surprising to see that there are currently more than 20,000 MW of gas-fired generation capacity in various stages of construction, planning or proposed across Australia. And according to recent forecasts by ABARE, electricity generated by gas will grow significantly over the next twenty years, tripling current levels.

Each of these power stations will require gas transportation and/or storage services, and APA is in the advantageous position of having the infrastructure in place, and the skills and experience to provide this.

These changes are good for APA, and for the environment, with the need for more gas, more gas-fired generation, and hence more pipeline capacity and services.

### **Building Australia's gas infrastructure**

In our 10 year history, we have been working closely with our customers to develop commercially viable, cost effective and efficient infrastructure solutions.

Across the country we are delivering gas and expanding our infrastructure, and in some cases building completely new infrastructure, to meet the growing demand for energy. Furthermore, we continue to improve and develop our services to match the dynamic and evolving Australian energy market.

This is presently happening effectively without government involvement or government subsidies. In fact, in this decade, all new pipelines, and pipeline expansions have been the result of commercial negotiations between customers and pipeline companies such as APA.

We see no need for the government to step in and start using tax payers dollars on an already well functioning system. A case in point is the possibility of Government support for building an electricity transmission line to Mt Isa mining operations.

The capital cost of the proposed Copper String transmission line from Townsville to Mt Isa is estimated to be in excess of \$1 billion, with government subsidies of more than \$0.5 billion needed to make it competitive with existing energy solutions.

Since Mt Isa has an existing electricity supply fuelled by natural gas that can be efficiently expanded at significantly less cost than building a new transmission line, we believe these government funds would be better applied elsewhere where there is no or limited electricity supply .

### **APA Sustainability report**

This year, we have produced our first sustainability report.

Our success has been built on strong financial performance, but also on our commitment to achieving our goals in relation to all our stakeholders – employees, customers, investors, the environment and the communities around us.

I'll focus on a few areas today – APA's people, safety and the environment.

I am especially proud of our people, who with their extensive commercial and operational skills and experience, are managing, growing and improving our business.

They are engaged, working with a great sense of ownership to deliver greater value to the business and to our customers.

As someone who has worked in every area of the business, I'm not blind to the risks faced each day by our people, and like me, I want them home safely to their loved ones every day.

So safety remains paramount to us and we remain vigilant on continuously improving our safety performance, with particular focus on early recognition and reporting of potential safety risks, working hard towards our long-term goal of 'Zero Harm'.

I'm happy to report that last year we improved our Loss Time Injury frequency rate from 7.3 to 4.9 and this year we are targeting a reduction to 4.0.

We are also committed to minimising the environmental impact of all our activities, conducting our operations efficiently and according to best practice standards, whether out in the field building or operating our assets, or in the office with the way we use and consume resources.

We are also active in encouraging the use of natural gas as it is a key fuel in reducing carbon emissions in a timely and cost efficient manner.

We continue to engage with government and industry associations to promote natural gas as a readily available and plentiful solution for a carbon-constrained economy.

APA will also continue playing a meaningful role in developing the infrastructure and services to encourage and enable gas use.

## **Conclusion**

We end APA's first decade of operation with a resilient and growing business, and remain well positioned to continue growing sustainably and profitably in 2011 and well beyond that into the future.

We have attractive investment opportunities due to the continued growth in gas demand and the scale and location of our assets across the country. And we have the internal expertise and the financial capability to take advantage of these opportunities.

As we start APA's new decade, we remain focused on our objective of maximising the value of APA's business and value for our securityholders. With APA's assets, people and financial strength, together with a growing demand for gas, I believe the best days for APA are ahead of us.

## **APA Group 2010 Annual Meeting Securityholders Questions and Answers**

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We invited securityholders to submit written questions on the form sent with the notice of meeting. We have already covered a number of the questions we received in my earlier address and the Managing Director's address, and I'd now like to respond to some other issues that have been raised.

### **Tax statements**

As occurred in previous years, we received questions about the tax statement being sent to securityholders in September.

As you may recall, in 2006 following APA's acquisition of GasNet, we adopted the stapled structure, joining the APT Investment Trust to Australian Pipeline Trust. This was done to increase flexibility in how distributions are paid to securityholders, for their benefit.

APT Investment Trust distributes income before tax to securityholders, so this income is taxed at securityholders' own marginal rates, rather than the taxable income of the trust being taxed at the top marginal rate of 46.5%.

However, a consequence of this is that securityholders must declare that income (this year received in September) in their 2010 tax return and some have expressed disappointment that they are unable to complete their tax returns until the tax statement is received.

Currently, the determination of the final distribution is based on the audited annual results, which were not finalised until the 25th August. In that regard APA's timetable is not out of step with similarly structured infrastructure businesses. While tax statements were sent in September, details of the distribution and its different components sufficient to allow the preparation of a tax return were published on the same day that the financial results were released, on the 25th August.

### **Remuneration report**

At APA, we are committed to disclosing a clear and transparent summary of our remuneration arrangements. This year our remuneration report reflects the recommendations of the Federal Government's response to the Productivity Commission's inquiry on executive remuneration. This includes providing clear summaries of remuneration policies and reporting on actual levels of remuneration received by directors and executives during the year, which can differ from the remuneration reported in the financial statements, that is remuneration earned in the year, as determined by relevant accounting standards.

There were no significant changes to remuneration structure or policies during the year. The overall aim remains to attract and retain a high calibre of directors and management who will create long-term, sustainable value for securityholders.

With this in mind, a significant part of executive remuneration is linked to a combination of financial measures and executives' individual key performance goals, with an even weighting between short term and long term incentives.

These incentives are designed to align the interests of executives with those of securityholders, including by the use of operating cash flow per security as the key performance hurdle for participation in the incentives, and by linking the reward under the long term incentive to the performance of the APA security price during the three year period over which that incentive vests.

The effectiveness of the remuneration strategy is exemplified by the financial performance and returns to securityholders that I spoke of in my earlier address.

### **Questions for the auditor**

On the form sent with the notice of meeting, we invited securityholders to submit questions to the auditor on the conduct of the audit or the content of the auditor's report. The auditor has advised that in their opinion none of the questions received relates to those issues. If however any of you here today have a question on the conduct of the audit or the content of the auditor's report, as I've mentioned our auditor is in attendance today and willing to take such questions, through me as Chairman of this meeting.

### **Compliments**

Finally, reading through the questions submitted by securityholders, I was again delighted to see the interest of securityholders in APA, with many thoughtful and interesting questions.

It was also gratifying for me to read the positive comments submitted, that reflected both securityholder support of the business, and affirmation of APA Board and staff in managing the business.

We have been encouraged to "please continue on, as we have this year and decade, to make good returns for securityholders".

I trust the information presented about APA at this year's Annual Meeting has shown that we have the right assets and the right people to continue to do just that.