AIRWAYS
making your world possible

Airways Interim Report
2018 ▸ 2019

For the period ended 31 December 2018

CONTENTS

"ELEVATION OF THE DRONE USER HUB AIRSHARE TO A SUBSIDIARY BUSINESS MARKS THE BEGINNING OF DEVELOPMENT OF AN UNMANNED AERIAL VEHICLE AIR TRAFFIC MANAGEMENT (UTM) SYSTEM FOR NEW ZEALAND."

SUMMARY OF PERFORMANCE

The first half of the 2018 – 2019 financial year delivered solid safety, operational and financial performance for Airways New Zealand. This reflects our absolute commitment to delivering safe and efficient air navigation services for New Zealand and beyond, as we work to shape the aviation environment of the future.

Airways' vision for predictive safety management ensures we are continually learning from events across the aviation industry and, as the aviation environment evolves, safety at Airways continues to adapt and improve. For the period ending 31 December 2018, Airways reported zero major severity health and safety events. Air traffic control loss of separation events have remained stable, however one near collision event was recorded. This involved two light aircraft in Rotorua.

New opportunities and a focus on fostering relationships in the Middle East and Asian markets have fuelled the success of Airways' subsidiary businesses, with revenue up 16% on the same period last year.

Elevation of the drone user hub AirShare to a subsidiary business marks the beginning of development of an unmanned aerial vehicle air traffic management (UTM) system for New Zealand. With 11,000 users logging more than 600 flights each week, AirShare has experienced significant growth over the past four years. This new structure will allow AirShare to develop a commercially viable service that safely integrates drones into the wider air traffic network, alongside our existing customers.

The AirShare business moved into new premises in late 2018 and began testing a pilot system that will replace the existing tool.

We continue to be concerned about the number of drones operating without authorisation in controlled airspace. In the six months to December 31, 2018, there were 53 airspace incursions by drones. In these cases, drones were flying close enough to aircraft or airfields to be sighted by pilots or air traffic controllers. In a number of these cases, airspace had to be closed for periods of up to half an hour to ensure the safety of other air traffic.

In October we began a trial of radar based drone detection technology at Auckland International Airport. The technology may have the capability to identify drones operating around airports, allowing air traffic controllers to notify pilots of any necessary action. The trial is expected to be ongoing throughout 2019 as we consider how the technology could be integrated into Airways' operating environment.

August saw the opening of new air traffic control towers at Wellington International Airport and Nelson Airport. These two modern towers are a significant investment for Airways and will support the growing aviation needs of both locations. They are likely to be the last two 'bricks and mortar' towers to open in New Zealand, as we look to digital air traffic control tower technology as a way to deliver safer and more efficient aerodrome services that are better aligned to our customers' needs.

During the period we continued with the procurement of a digital tower solution for Invercargill Airport – New Zealand's first digital tower, due to go live in 2020.

Construction of the new Auckland and Christchurch Air Traffic Centres is progressing well. Both centres are on track for commissioning in 2020 when our new $58 million ATM platform will become operational, bringing increased safety and efficiency benefits.

Airways' first sustainability framework launched in September. The framework sets out how we will achieve our strategic goals in a socially and environmentally sustainable way that works for us, our people and communities.

Measures of success	FY19 actual YTD	FY19 plan YTD	FY18 actual YTD
Near collisions	1	Nil	Nil
Critical technology services availability	99.99%	99.95%	99.95%
Group NOPAT	13.5m	11.8m	13.9m[1]
Commercial business NOPAT	3.7m	3.8m	3.4m
Capital investment	20.8m	35.4m	21.5m

1 Excludes a $4.2 million gain on the sale of land in July 2017.

FINANCIAL PERFORMANCE

The Airways group reported a net operating profit after tax (NOPAT) of $13.5 million for the half year, broadly in line with the prior year's $13.9 million and $1.7 million ahead of budget. The result has been driven by increasing air traffic volumes and continued growth in profits from our commercial businesses.

Flight volumes within the core business have continued to increase on both domestic and international routes, with year to date volumes up 1.9% on budget and 2.4% on the prior year. Core business costs are tracking behind plan for the first six months, although this variance is expected to unwind by year end with the initiation of a number of planned initiatives and projects.

Capital investment in key projects is progressing well and, although overall spend for the first six months is below budget, commitments to customers for the 2017-2019 pricing round are on track to be delivered. Investment in two large projects outside the original pricing plan – lighting for a new flexible contingent runway in Auckland and the development of a digital tower at Invercargill Airport – is now likely to occur in future years.

The commercial businesses have maintained the steady growth of recent years, with revenue up 16% on the same period last year. This growth is coming from across the portfolio, with significant contributions to the December 2018 result coming from procedure design work in the Philippines and the commencement of a new training partnership in Kuwait. Good progress has also been made on the development and installation of a simulator in Lebanon, although revenue will not be recognised until later in the financial year.

The increased volume of activity within the commercial business, particularly delivering projects with large equipment components, is driving an increase in operating expenses from the prior year. However, this has been offset by corresponding increases in revenue.

The full year group NOPAT forecast remains in line with our Statement of Corporate Intent target of $23.4 million.

OUR PEOPLE

In a rapidly changing and increasingly complex airspace environment, Airways has continued to maintain safe and efficient air traffic control and operations across 30 million square kilometres of South Pacific airspace, and to the highest of industry standards. I would like to thank Airways' people for their hard work and commitment to achieving this.

Graeme Sumner
Chief Executive Officer

STATEMENT OF COMPREHENSIVE INCOME

(all figures shown in tables are in $NZ thousands unless otherwise stated)

	GROUP		
FOR THE PERIOD ENDED 31 DECEMBER	Dec 2018 Unaudited	Dec 2017 Unaudited	NOTES
OPERATING ACTIVITIES			
REVENUE			
Air traffic management revenue	102,256	97,552	
Net gain on sale of assets	1	4,185	3
Other revenue	12,095	9,856	
TOTAL REVENUE	**114,352**	**111,593**	
EXPENSES			
Employee remuneration	57,291	54,393	8
Employee related costs	3,969	3,732	
Depreciation	9,832	8,943	
Amortisation	2,233	2,522	
Other operating costs	18,080	15,735	4
Rental expense on operating leases	3,906	2,801	
Net finance expense	323	90	5
TOTAL EXPENSES	**95,634**	**88,216**	
NET SURPLUS BEFORE TAXATION	**18,718**	**23,377**	
Taxation expense	5,241	5,314	
NET SURPLUS AFTER TAXATION ATTRIBUTABLE TO EQUITY SHAREHOLDERS	**13,477**	**18,063**	
OTHER COMPREHENSIVE INCOME			
That will be reclassified to profit or loss when conditions are met:			
Movement in cash flow hedge reserve	1	439	
Deferred tax on other comprehensive income	–	(123)	
TOTAL OTHER COMPREHENSIVE INCOME	**1**	**316**	
TOTAL COMPREHENSIVE INCOME FOR THE YEAR ATTRIBUTABLE TO EQUITY SHAREHOLDERS	**13,478**	**18,379**	

This statement is to be read in conjunction with the Notes to the Financial Statements on pages 08-10.

STATEMENT OF CHANGES IN EQUITY

(all figures shown in tables are in $NZ thousands unless otherwise stated)

	GROUP ATTRIBUTABLE TO EQUITY SHAREHOLDERS				
	Contributed Equity	Hedge Reserve	Retained Profits	Total	Notes
BALANCE AS AT 1 JULY 2017	41,100	(2,080)	76,318	115,338	
COMPREHENSIVE INCOME					
Net surplus after taxation	–	–	18,063	18,063	
OTHER COMPREHENSIVE INCOME					
Movements in hedge contracts	–	439	–	439	
Deferred tax on other comprehensive income	–	(123)	–	(123)	
TOTAL OTHER COMPREHENSIVE INCOME	**–**	**316**	**–**	**316**	
TOTAL COMPREHENSIVE INCOME	**–**	**316**	**18,063**	**18,379**	
TRANSACTIONS WITH OWNERS					
Dividends paid (7.3 cents per share)	–	–	(3,000)	(3,000)	6
TOTAL TRANSACTIONS WITH OWNERS	**–**	**–**	**(3,000)**	**(3,000)**	
BALANCE AS AT 31 DECEMBER 2017	**41,100**	**(1,764)**	**91,381**	**130,717**	
BALANCE AS AT 1 JULY 2018	**41,100**	**(1,223)**	**92,475**	**132,352**	
COMPREHENSIVE INCOME					
Net surplus after taxation	–	–	13,477	13,477	
OTHER COMPREHENSIVE INCOME					
Movements in hedge contracts	–	1	–	1	
Deferred tax on other comprehensive income	–	–	–	–	
TOTAL OTHER COMPREHENSIVE INCOME	–	1	–	1	
TOTAL COMPREHENSIVE INCOME	–	1	13,477	13,478	
TRANSACTIONS WITH OWNERS					
Dividends paid (9.7 cents per share)	–	–	(4,000)	(4,000)	6
TOTAL TRANSACTIONS WITH OWNERS	–	–	(4,000)	(4,000)	
BALANCE AS AT 31 DECEMBER 2018	41,100	(1,222)	101,952	141,830	

CHIEF EXECUTIVE'S REPORT

FINANCIAL STATEMENTS

EVA KEY PERFORMANCE INDICATOR

CORPORATE DIRECTORY

This statement is to be read in conjunction with the Notes to the Financial Statements on pages 08-10.

INTERIM BALANCE SHEET

(all figures shown in tables are in $NZ thousands unless otherwise stated)

	GROUP			
FOR THE PERIOD ENDED 31 DECEMBER	Dec 2018 unaudited	Jun 2018 audited	Dec 2017 unaudited	NOTES
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents	5,567	1,750	5,718	7
Trade and other receivables	27,890	25,618	27,646	
Prepayments	2,834	2,150	2,548	
Derivative financial instruments	166	172	69	
TOTAL CURRENT ASSETS	**36,457**	**29,690**	**35,981**	
NON-CURRENT ASSETS				
Property, plant and equipment	188,368	176,707	164,606	9
Assets held for sale			98	
Intangibles	19,648	22,491	21,128	9
Inventory	1,628	1,581	1,429	
Other non-current assets	84	84	84	
Derivative financial instruments	2	55	2	
TOTAL NON-CURRENT ASSETS	**209,730**	**200,918**	**187,347**	
TOTAL ASSETS	**246,187**	**230,608**	**223,328**	
LIABILITIES				
CURRENT LIABILITIES				
Trade and other payables	17,348	16,778	12,771	
Employee entitlements	18,534	19,350	17,096	8
Current tax liability	2,424	4,312	2,326	
Derivative financial instruments	372	519	185	
TOTAL CURRENT LIABILITIES	**38,678**	**40,959**	**32,378**	
NON-CURRENT LIABILITIES				
Loan facility - unsecured	48,000	40,000	40,000	
Deferred tax liability	8,269	8,345	8,990	
Employee entitlements	7,885	7,518	8,938	8
Derivative financial instruments	1,525	1,435	2,305	
TOTAL NON-CURRENT LIABILITIES	**65,679**	**57,298**	**60,233**	
TOTAL LIABILITIES	**104,357**	**98,257**	**92,611**	
NET ASSETS	**141,830**	**132,351**	**130,717**	
EQUITY				
Share Capital	41,100	41,100	41,100	
Reserves	(1,222)	(1,223)	(1,764)	
Retained Earnings	101,952	92,474	91,381	
TOTAL EQUITY	**141,830**	**132,351**	**130,717**	

This statement is to be read in conjunction with the Notes to the Financial Statements on pages 08-10.

INTERIM STATEMENT OF CASH FLOWS

(all figures shown in tables are in $NZ thousands unless otherwise stated)

	GROUP		
FOR THE PERIOD ENDED 31 DECEMBER	Dec 2018 Unaudited	Dec 2017 Unaudited	NOTES
CASH FLOWS FROM OPERATING ACTIVITIES			
CASH WAS PROVIDED FROM:			
Receipts from customers	114,808	103,708	
Interest received	5	14	
CASH WAS APPLIED TO:			
Payments to suppliers	(23,535)	(19,081)	
Payments to employees	(63,096)	(59,471)	
Interest paid	(282)	(64)	
Income tax paid	(7,205)	(5,098)	
NET CASH FLOWS FROM OPERATING ACTIVITIES	**20,695**	**20,008**	12
CASH FLOWS FROM INVESTING ACTIVITIES			
CASH WAS PROVIDED FROM:			
Sale of property, plant and equipment	–	7,226	3
CASH WAS APPLIED TO:			
Purchase of property, plant and equipment	(14,293)	(14,752)	
Purchase of intangible assets	(6,585)	(6,286)	
NET CASH FLOWS FROM INVESTING ACTIVITIES	**(20,878)**	**(13,812)**	
CASH FLOWS FROM FINANCING ACTIVITIES			
CASH WAS PROVIDED FROM:			
Drawdown of loan facility	8,000	1,000	
CASH WAS APPLIED TO:			
Payment of dividends	(4,000)	(3,000)	6
NET CASH FLOWS FROM FINANCING ACTIVITIES	**4,000**	**(2,000)**	
NET INCREASE IN CASH HELD	**3,817**	**4,196**	
Cash at the beginning of the period	1,750	1,522	
CASH AT THE END OF THE PERIOD	**5,567**	**5,718**	

Interest paid above excludes capitalised interest. Total interest paid for the period was $1,007 (2017: $1,213).

CHIEF EXECUTIVE'S REPORT
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CORPORATE DIRECTORY

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NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 BASIS OF PREPARATION

These interim financial statements as at and for the six months ended 31 December 2018 are for the consolidated group (Airways), consisting of Airways Corporation of New Zealand Limited and its subsidiaries: Airways International Limited, Aeropath Limited, Airways Training Limited and Airshare Limited. They have been prepared in accordance with:

- Generally Accepted Accounting Practice in New Zealand and NZ IAS 34, 'Interim Financial Reporting' (as a result they comply with the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards, as appropriate for profit-oriented and tier 1 entities. They also comply with International Financial Reporting Standards); and
- The requirements of the Financial Reporting Act 2013, Companies Act 1993 and the State-Owned Enterprises Act 1986.

The interim financial statements have been prepared on the historical cost basis as modified by the revaluation of derivative financial instruments and are presented in New Zealand dollars, which is Airways' presentation currency and the functional currency of all entities within the group. All values are rounded to the nearest thousand dollars ($'000) unless otherwise stated.

The following standards with an impact on Airways have been adopted in the current accounting period:

NZ IFRS 15 - 'Revenue from Contracts with customers', issued in July 2014 (effective for periods beginning on or after 1 January 2018). A full retrospective approach has been taken to adoption but no changes were required to the comparative balances. The impact on of the application of this standard has been minimal.

NZ IFRS 9 – 'Financial Instruments', issued November 2012 (effective for periods beginning on or after 1 January 2018). The application of this standard has not resulted in the restatement of comparatives and has had minimal impact.

All components in the primary statements have been stated net of GST, with the exception of receivables and payables which include any GST invoiced.

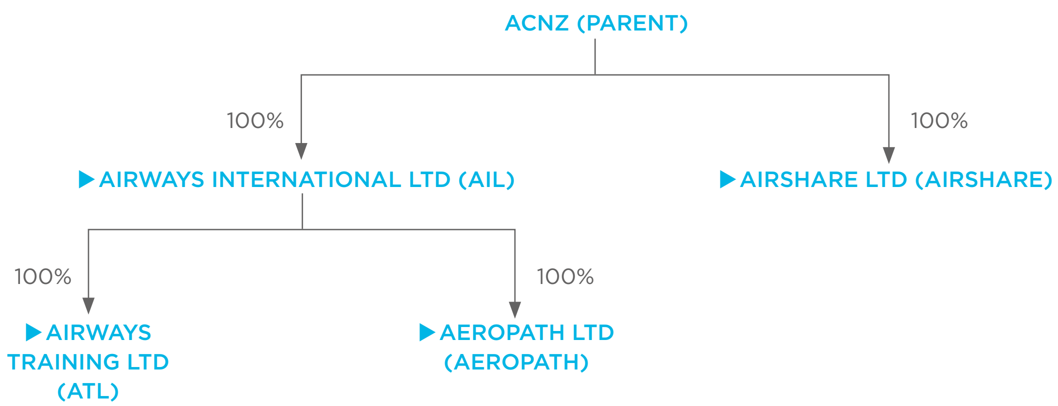
These interim financial statements should be read in conjunction with the 2018 Annual Report.

NOTE 2 GROUP STRUCTURE

Airways Corporation of New Zealand Limited is a limited liability company incorporated and domiciled in New Zealand. It is also a State-Owned Enterprise established under the State-Owned Enterprises Act 1986 with shares held in equal numbers by the Minister for State-Owned Enterprises and the Minister of Finance, on behalf of the Crown.

Airways' principal business is the provision of air traffic management services; however, it is also involved in a number of related revenue generating activities, including consulting and training.

The group structure is shown in the diagram below. The percentages indicate ownership.



NOTE 2 GROUP STRUCTURE CONT.

Entity	Principal activity
Airways International Ltd	Revenue management, recruitment and training, and air navigation services and maintenance of systems
Airways Training Ltd	Aviation English Training
Aeropath Ltd	Aeronautical information management and procedural design and development services.
Airshare Ltd	A new entity incorporated 16 November 2018 to deliver unmanned aerial vehicle (UAV) and drone traffic management services (currently not trading)

NOTE 3 NET GAIN ON SALE OF ASSETS

Net gain on sale of assets is nil (2017: $4.4 million). 2017 included a gain on the sale of a parcel of land in Queenstown.

NOTE 4 OTHER OPERATING COSTS

Other operating costs are up on the prior year as a result of the equipment costs incurred in delivering commercial business projects. These additional costs are offset by the corresponding increase in revenue.

NOTE 5 NET FINANCE EXPENSE

Net finance expense of $0.324 million includes financing expenses of $1.226 million offset by capitalised interest of $0.902 million (2017: $0.09 million net).

NOTE 6 DIVIDENDS PAID

A $4 million interim dividend has been delivered to shareholders over the reporting period. Airways expects to pay a total dividend of $12 million for the full year to 30 June 2019.

NOTE 7 CASH AND CASH EQUIVALENTS

Airways operates an overdraft facility to manage operational cash flow without the requirement to hold surplus cash on hand. The overdraft facility incurs interest rates on similar terms as long term borrowings and represents a critical component of Airways' liquidity risk management strategy.

NOTE 8 EMPLOYEE ENTITLEMENTS

Employee entitlements (current and non-current) is largely made up of accrued salary costs, annual leave, long service leave and retiring leave liabilities.

NOTE 9 CAPITAL COMMITMENTS

Airways had total capital commitments of $74.3 million as at 31 December 2018 ($86.6 million as at 31 December 2017). This programme will be funded through operating cash flow and increased debt, while remaining within current loan facilities and covenants.

NOTE 10 CONTINGENT LIABILITIES

Airways has contingent liabilities of $1.383 million for performance bonds (2017: $0.449 million).

NOTE 11 SUBSEQUENT EVENTS

There have been no significant events occurring since balance date requiring disclosure.

NOTE 12 RECONCILIATION OF THE NET CASH FLOW FROM OPERATING ACTIVITIES TO REPORTED PROFIT

(All figures shown in tables are in $NZ thousands unless otherwise stated)

FOR THE PERIOD ENDED 31 DECEMBER	Dec 2018	Dec 2017
NET SURPLUS AFTER TAXATION	13,477	18,063
ADD NON CASH ITEMS		
Accounting gain on sale of assets	–	(4,185)
Amortisation	2,233	2,522
Depreciation and impairment	9,832	8,943
Movement in deferred tax	(77)	–
Share of loss/(profit) from joint venture	–	–
TOTAL ADJUSTMENTS FOR ITEMS IN SURPLUS NOT IMPACTING CASH FLOW	**11,988**	**7,280**
ADD MOVEMENTS IN WORKING CAPITAL ITEMS		
Increase/(decrease) in payables	(1,769)	(418)
Decrease/(increase) in receivables	(3,001)	(4,917)
TOTAL ADJUSTMENTS FOR ITEMS NOT IN SURPLUS IMPACTING CASH FLOW	**(4,770)**	**(5,335)**
NET CASH INFLOW FROM OPERATING ACTIVITIES	**20,695**	**20,008**

EVA KEY PERFORMANCE INDICATORS

(All figures shown in tables are in $NZ thousands unless otherwise stated)

FOR THE PERIOD ENDED 31 DECEMBER	PARENT Dec 2018	PARENT Dec 2017
DEBT AND EQUITY EMPLOYED		
Debt employed	87,742	74,985
Equity employed	143,637	140,539
TOTAL DEBT AND EQUITY EMPLOYED	**231,379**	215,524
Charge on operating capital	7,415	6,938
Economic Value Added	3,555	3,491
SUMMARY OF PARAMETERS FOR COST OF CAPITAL		
Risk free rate – three-year Government Stock	1.82%	2.07%
Market risk premium	7.0%	7.0%
Company tax rate	28.0%	28.0%
Business risk factor (asset beta)	0.60	0.60
Cost of capital	6.59%	6.74%

EVA measures the extent to which a business is performing above or below expectations. A positive EVA means the business is adding value after allowing for a normal reward to the providers of capital. The EVA reporting framework applied by Airways can be found at the following website:

https://www.airways.co.nz/about/financial-operational-and-safety-performance-reports/

Consistent with the previous year, Airways' parent company EVA result of $3.6 million for the six months to December 2018 is expected to reduce in the second half of the financial year. Air traffic volumes have a seasonal weighting to the first six months, while capital expenditure and associated interest and depreciation costs are weighted to the second half of the year.

The cost of capital of 6.59% for the period ending December 2018 compares to a cost of capital of 6.90% used for determining 2017–19 air navigation services pricing. The movement in the cost of capital is due to changes in the risk free rate.

RECONCILIATION OF EVA TO NET OPERATING PROFIT AFTER TAX

FOR THE PERIOD ENDED 31 DECEMBER	PARENT Dec 2018	PARENT Dec 2017
NOPAT	9,784	14,658
Deduct: Charge on operating capital	(7,415)	(6,938)
Deduct: Queenstown land sale	0	(4,263)
Deduct: non-cash employee costs	960	(136)
Deduct: movement in deferred taxation	(157)	(106)
Add back: interest costs	383	276
Economic Value Added	**3,555**	**3,491**

CORPORATE DIRECTORY

Directors

Judy Kirk (ceased 31/12/2018)
Denise Church (appointed 1/1/2019)
Mary-Jane Daly
Darin Cusack
Lisa Jacobs (appointed 1/11/2018)
Paula Jackson (appointed 1/1/2019)
John Holt (appointed 1/1/2019)
Bennett Medary
Dr Chris Moxon (ceased 31/10/2018)
Mark Pitt

Registered office

Level 7
Majestic Centre
100 Willis Street
PO Box 294
Wellington
New Zealand

Web address

www.airways.co.nz

Auditors

Kevin Brown, with the assistance of PricewaterhouseCoopers on behalf of the Auditor-General

Bankers

ANZ Bank New Zealand Limited
Bank of New Zealand Limited

insightcreative.co.nz

airways.co.nz