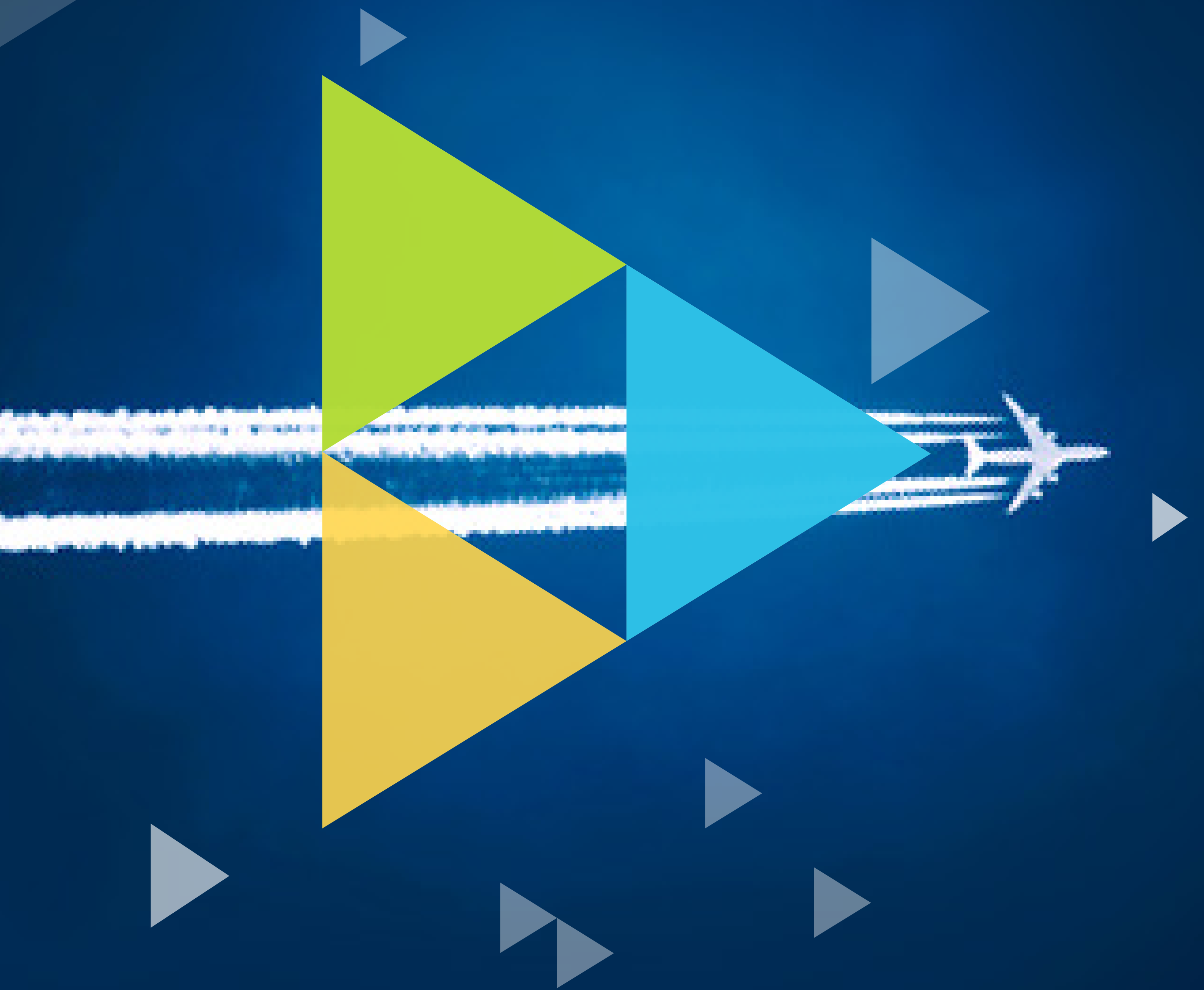
AIRWAYS



STATEMENT OF CORPORATE INTENT

FY19 ▸ FY21

Contents

CONTENTS

Introduction

Airways Corporation of New Zealand Limited (ACNZ) is a state-owned enterprise (SOE) established under the State-Owned Enterprise Act 1986 (the Act) and is a public company registered under the Companies Act 1993. The shareholders are the Minister for State-Owned Enterprises and the Minister of Finance, each of whom holds 20.55 million fully paid shares of $1.

Airways' core role is as New Zealand's air traffic control (ATC) provider, facilitating safe and efficient air transport through New Zealand's flight information region (FIR). ACNZ also has three 100% owned subsidiaries – Airways International Limited, Airways Training Limited and Aeropath Limited.

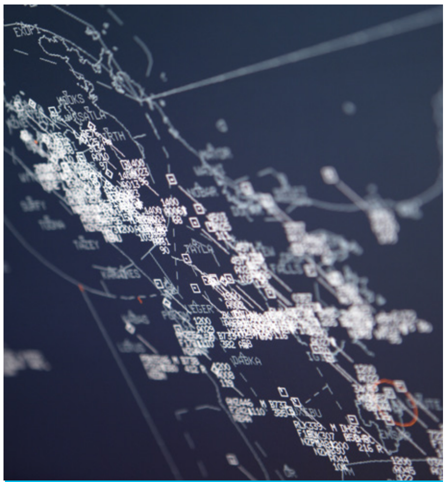
This Statement of Corporate Intent (SCI) refers to the Airways Group (Airways), including ACNZ and our subsidiaries. It is prepared in accordance with the Act and sets out Airways' business goals and objectives for the period 1 July 2018 to 30 June 2021.

OBJECTIVES, MISSION, PURPOSE AND VALUES

As an SOE, Airways' primary objectives are to:

- be as profitable and efficient as comparable businesses
- be a good employer
- exhibit a sense of social responsibility

In recognition of these objectives, Airways has established these mission, purpose and values:



MISSION
Build a progressive airspace environment that enables aviation to thrive

PURPOSE
To be safe, successful and sustainable

VALUES
We value safety, each other, excellence and success

Strategic context

We pride ourselves on being one of the world's safest, most efficient and most innovative air traffic management (ATM) service providers. We use capability and experience to turn industry change into growth opportunities.

Increasingly, the traditional ATM model based on sovereign provision, ground-based surveillance and proprietary systems is under disruption at every stage of the value chain. Advances in satellite-based surveillance and digital technology are breaking down traditional barriers to entry, but are also creating opportunities for safer and more efficient ATM services. With the centre of air travel forecast to move towards Asia Pacific over the coming two decades, the New Zealand aviation industry will need innovative solutions to manage this technological and cultural change.

Reflecting these trends, Airways refreshed and refined our long-term strategy in 2016/17, developing a blueprint for the future state of Airways – a future focused on long-term network optimisation and value creation.

This blueprint for the future is bigger than just New Zealand's airspace. It promotes Airways as a global leader that is fundamentally safe and commercially viable. Airways aims to influence the entire airspace environment – ATC, airlines, airports, government, industry and tourism – by adopting the following five strategies.

THIS BLUEPRINT FOR THE FUTURE IS BIGGER THAN JUST NEW ZEALAND'S AIRSPACE. IT PROMOTES AIRWAYS AS A GLOBAL LEADER THAT IS FUNDAMENTALLY SAFE AND COMMERCIALLY VIABLE.

1	2	3	4	5
ENHANCE SAFETY CULTURE	**GROW CAPABILITY**	**INVEST AND INNOVATE**	**SIMPLIFY OUR BUSINESS**	**GROW AND DIVERSIFY**
Embed proactive risk prevention and safety practices within a maturing Just Culture	Build an accountable and performance-focused organisational culture	Adapt to an evolving ATM environment, leverage technology to deliver value to customers	Utilise data and technology changes to move to an "electronic way of being"	Diversifying sources of revenue beyond core customers

Airways' business units

Airways is an air navigation service provider (ANSP) responsible for delivering ATM services within New Zealand and internationally.

Airways' business model comprises two business units described in the table below:

	CORE BUSINESS	COMMERCIAL BUSINESSES
Purpose	▶ Deliver safe, resilient and efficient ATM services to NZ airspace users ▶ Long-term investment focus delivering modern and flexible solutions to current and future customers	▶ Utilise Airways' IP and expertise to provide products and services to the international ANSP and wider aviation industry ▶ Create value by investing in a balanced portfolio, operating internationally and achieving commercial returns
Business scope	▶ **Air traffic control services:** separation of aircraft in flight, to standards determined by the appropriate regulatory authority (NZ Civil Aviation Authority) ▶ **Air traffic management services:** management of aircraft to maximise network capacity and reduce fuel burn and carbon emissions through optimised aircraft flight paths	▶ **Airways Training:** delivering ATC training services through partnership and across multiple platforms ▶ **Airways Digital:** utilising cloud-based technologies to support ANSPs with air traffic management, revenue management, recruitment and selection, workforce planning and training ▶ **Aeropath/Aviation Services:** offering specialised aeronautical information management, procedure design and electrical and engineering services
Funding model	▶ Governed by a Service and Pricing framework which provides for a 'fair return on investment' ▶ Customers are engaged on a tri-annual pricing consultation	▶ Autonomous business units charged with delivering commercial returns ▶ Reinvesting a portion of the net operating profit after tax (NOPAT) into new products and innovation

CORE BUSINESS

Airways' primary purpose is to deliver ATM services within New Zealand. This role has evolved from a traditional, safe separation function to an aviation system enabler, optimising traffic flows across the aviation network.

To deliver on this concept, Airways has embarked on a 10-year operational strategy, designed to deliver quantum improvements in the safety, resilience and efficiency of our ATM services. This strategy will see Airways operating state of the art technology and systems, from two interoperable centres.

The key components of this strategy for FY2018/19 include:

- continue implementation of a single air traffic management platform, replacing the aging domestic and oceanic systems
- commence training on a standardised set of operating procedures for combined terminal operations
- commence construction of two new seismically-resilient operational facilities in Auckland and Christchurch
- investment in R&D to optimise service efficiency

New Zealand's Flight Information Region

Airways provides services to domestic and international air traffic within New Zealand's FIR which totals 30 million square kilometres – one of the largest areas of sovereign airspace in the world. Within this FIR, Airways controls approximately 1.1 million aircraft movements per year.

Core services

Airways' core business comprises the following key air traffic services.

- Enroute and approach services within New Zealand's FIR. These services are covered by statute and represent ~60% or $120 million of core revenue.
- Enroute services in the Auckland Oceanic FIR. These are provided on behalf of the International Civil Aviation Organization (ICAO) and represent ~15% or $30 million of core revenue.
- Aerodrome services at New Zealand airports (air traffic control into and out of aerodromes and provision of lighting and navigation infrastructure for airfields). Represent ~25% or $50 million of core revenue.

Airways' core business customers

Airways is committed to working with aviation customers and stakeholders in enabling a safe and efficient aviation network. Major customer groups are:

- airlines and commercial aircraft operators
- general aviation
- the Royal New Zealand Air Force
- airports

COMMERCIAL BUSINESSES

In an increasingly liberalised operating environment, Airways' commercial businesses deliver high quality services, innovative products and competitive pricing to the global ANSP and aviation industry. They provide portfolio diversification and growth opportunities for the Group, and are managed independently of the statutory business. The higher returns provided by these businesses enhance shareholder value and provide options for reinvestment or dividend distribution.

The vision for the commercial businesses is to deliver high value products and services that meet the unique and complex needs of the ANSP and aviation industry. This will occur by capitalising on the global drive for reduced ANSP operating costs and the potential for outsourcing, product unbundling and consolidation in the traditional ANSP model.

In the longer term, the target product and service mix will be software-based (utilising a subscription or license revenue model); highly scalable (built on a model of 'build it once and sell it many times') and able to deliver long term, repeatable revenue streams. Over time, it will also focus on potentially higher value sectors in the aviation industry including airlines and airports.

Investment is required within the commercial portfolio to ensure it is balanced and capable of generating short, medium and long-term value. This investment will be both back into the existing businesses to support the continued development of the product and service mix, and into strategic partners that will generate intellectual property (IP) for commercial gain and enhance the core business.

The three primary businesses within the commercial portfolio are:

BUSINESS	PRODUCTS AND SERVICES
Airways Training	▶ Domestic campuses supporting New Zealand-based ATC training for Airways and international ANSPs ▶ International campuses run in conjunction with in-country partners
Airways Digital	▶ Airbooks: an online training platform supporting elearning tools ▶ Total Control: design, installation and maintenance of ATC simulators ▶ Sure Select: an ATC recruitment selection platform ▶ FlightYield: Modularised revenue management system
Aeropath/Aviation Services	▶ Next generation aeronautical design and information management ▶ Procedure design services, focused on performance-based navigation ▶ Aviation consultancy, equipment installation and maintenance services

GOVERNANCE

Safety & Assurance

Safety is paramount throughout the aviation industry, with continuous improvement in safe travel and operations a key priority for all participants. Against this backdrop, Airways keeps safety at the forefront of all we do and has established a proven track record of excellent safety results among our peers. The Safety & Assurance team provides a leadership role across the organisation in safety management, performance, measurement and maturity, and Just Culture. It also provides related assurance and advisory services to a range of internal and external stakeholders.

Safety & Assurance is leading improvements to support the vision of becoming predictive in safety: moving from reactive to proactive and then to predictive practices; learning through what could happen, as well as what has happened; and tailoring improvements in system design to ensure the best return on investment.

Corporate Services

Corporate Services provides quality advice to the business to support growth while ensuring risk is managed within Shareholder and Board-approved mandates. Services are structured functionally in the form of People, Finance, Legal, Public Affairs and Strategy teams to create value and protect Airways' brand.

The overarching vision for Corporate Services is to act as the trusted advisor to the Airways' Board, management and staff. Value is delivered to the business through a fit-for-purpose service offering which provides comprehensive advice and judgement, within a robust governance framework.

AIRWAYS CONTROLS APPROXIMATELY

1.1M

AIRCRAFT MOVEMENTS PER YEAR

FY19 key strategic workstreams

FY19 KEY STRATEGIC WORKSTREAMS

The key workstreams Airways will progress during FY19, and the initiatives and activities that will enable them, are set out in the table below.

FY19 KEY STRATEGIC WORKSTREAMS	FY19 INITIATIVES AND ACTIVITIES
Implement operations roadmap	▶ Complete the transition of Raglan enroute sector operations to Auckland ▶ Combine and consolidate Akld/Wgtn and Queenstown/Southern terminal operations ▶ Implement lower South Island surveillance approach
Deliver next generation ATM infrastructure	▶ Complete the new ATM system (Skyline X) software build ▶ Complete construction of new Christchurch and Auckland operational facilities ▶ Procure and install new voice switching systems in Auckland and Christchurch
Enhance organisational culture	▶ Implement and embed the new culture development plan
Invest in product development	▶ Source and validate new product opportunities that support strategy objectives ▶ Invest in training technology tools: bring AES into airbooks, simulator voice recognition
Technology partnering	▶ Initiate a strategic technology partnership to deliver an outsourcing capability ▶ Embed new Projects and Planning structure, including commercial management capability
Refresh commercial business customer engagement model	▶ Establish an integrated commercial business with a sustainable growth agenda ▶ Embrace a digital way of being that offers products and services on demand ▶ Develop an integrated sales strategy across all product and business lines
Develop digital aerodrome services capability	▶ Develop detailed concept of operations for nationwide digital aerodrome services ▶ Implement technical solution for Invercargill ▶ Develop an operating model for Auckland and one low volume aerodrome ▶ Submit safety case to the Civil Aviation Authority (CAA)
Develop UTM and drone solution	▶ UTM concept of operations defined and national system rollout underway ▶ Trial key underlying technology to enable beyond visual line-of-sight operations ▶ Develop concept of operations for Auckland CBD and work with CAA to implement
CSR and sustainability	▶ Develop a sustainability framework aligned with Airways' strategy

Performance targets and measures

MEASURES OF SUCCESS

	FORECAST FY18	PLAN FY19	PLAN FY20	PLAN FY21
OPERATIONAL				
▶ Near collisions	1	Nil	Nil	Nil
▶ Core systems availability	100%	100%	100%	100%
▶ Critical technology services availability	99.95%	99.95%	99.95%	99.95%
CUSTOMER				
▶ Core business customer satisfaction	81%	>80%	>80%	>80%
▶ Commercial customer satisfaction	97%	>80%	>80%	>80%
LEADERSHIP AND PEOPLE				
▶ Staff safety – serious harm injuries	Nil	Nil	Nil	Nil
▶ Staff engagement	65%	>FY18	>FY19	>FY20
FINANCIAL ($M)				
▶ Group NOPAT	27.1[1]	23.4	29.0	31.2
▶ Commercial business NOPAT	5.8	7.6	8.1	8.4
▶ Capital investment	47.8	71.7	73.0	55.2
▶ Dividends	11.0	12.0	13.0	14.0

1. Includes one off property gain of $4.2m

FINANCIAL FORECASTS BY UNIT ($NZM)

Airways expects to deliver a full year group NOPAT result of $27.1m for FY2017/18, in line with budget and SCI targets and ahead of the prior year.

Core business NOPAT is forecast to reach $21.3m, including a $4.2m gain on sale of land, with flight volumes slightly ahead of the estimates used to determine FY17/18 pricing and operating costs in line with budget.

The commercial businesses are forecast to deliver a NOPAT result of $5.8m, up on the prior year result of $5.2m but below budget. The portfolio has benefited from the restructure implemented in the previous year, with the businesses now operating with reduced overheads and more autonomy, and a strong year for ATC training services both in New Zealand and internationally.

Financial budgets for the three years from FY2018/19 are set out below.

REVENUE (Includes internal revenue)	FORECAST FY18	PLAN FY19	PLAN FY20	PLAN FY21
▶ Core business	**189.4**	**196.2**	**213.4**	**223.6**
COMMERCIAL BUSINESSES				
▶ Digital	2.2	4.4	4.8	5.2
▶ Aeropath/Aviation Services	23.2	23.5	23.5	23.5
▶ Training course delivery	9.1	10.9	11.2	11.5
	34.5	**38.8**	**39.5**	**40.2**
Group revenue	**223.9**	**235.0**	**252.9**	**263.8**
NOPAT				
▶ Core business	**21.3**[2]	**15.8**	**20.9**	**22.8**
COMMERCIAL BUSINESSES				
▶ Digital	0.2	0.2	0.5	0.8
▶ Aeropath/Aviation Services	3.1	4.0	4.0	4.0
▶ Training course delivery	2.5	3.4	3.6	3.6
	5.8	**7.6**	**8.1**	**8.4**
GROUP NOPAT	**27.1**	**23.4**	**29.0**	**31.2**

KEY FINANCIAL METRICS				
▶ Capital investment	47.8	71.7	73.0	55.2
▶ Group FTEs	782.0	792.1	789.1	789.1
▶ Group return on capital (GAAP)	21.8%	16.9%	19.1%	18.5%

Airways prepares financial statements in accordance with GAAP, with a complete list of accounting policies provided in Appendix A. The financial forecasts set out above comply with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards (as appropriate for profit-oriented entities) except for revenue, which is determined at the individual business unit level. As a result, the Group revenue number above includes internal revenue earned by Airways' commercial businesses from the statutory business. This internal revenue is eliminated in the annual financial statements, which are prepared at a Group level only. This has no impact on Group NOPAT.

Airways also uses Economic Value Added (EVA) principles to guide pricing decisions. Further detail is provided in Appendix C.

2. Included one off property gain of $4.2m.

DIVIDENDS

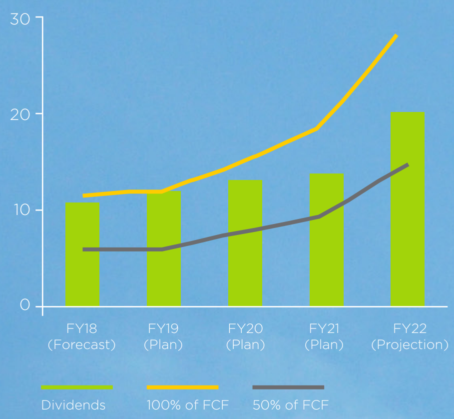
The Directors will seek to return a dividend of between 50% and 100% of Base Free Cash Flow from the Group (normalised for maintenance levels of capital investment), subject to targeting a Group gearing ratio below 35% over the medium term[3], while giving consideration to the performance of the business and changing financial conditions. Actual dividend payments will also remain subject to both solvency test and banking covenant restrictions.

In determining dividend levels, the Board will balance the objective of providing stable or increasing dividends to the Shareholder against short-to-medium term investment requirements and prudent risk management.

Specific dividend forecasts for the planning period, with respect to base free cashflow parameters, are set out below. Gearing is forecast to remain below 40% over the five years from FY18, with an average of 35%, within policy limits.

The level of dividend will be reviewed annually as part of the business planning process and at each declaration date. Dividends are usually paid in October and February and a final dividend not later than 30 June of each year.

DIVIDENDS VS FREE CASHFLOW LIMITS ($M)



3. Dividends are payable where average gearing over the next five-year period remains below 35% and there is no individual year where gearing exceeds 40%.

Corporate and social responsibility

Here are our current CSR/sustainability initiatives and areas of focus. Through FY19, we will review these initiatives to ensure our focus is aligned with Airways' strategy, and establish meaningful goals and targets

ENVIRONMENTAL SUSTAINABILITY

WHAT WE DO

Contribute to reductions in aviation industry carbon emissions

HOW WE DO IT

- Develop fuel efficient flight paths using performance-based navigation technologies (PBN), in consultation with airports, airlines and communities
- Actively partner with airports and airlines to support fuel efficient aircraft arrival and departure scheduling

SOCIAL RESPONSIBILITY

WHAT WE DO

Support our community

HOW WE DO IT

- Free ATC services and technical support for a two-week aviation scout camp
- Community scholarship programmes for safety initiatives, flying lessons and initiatives aimed at encouraging youth into engineering careers
- Fee waivers for community organisations

Support our people

HOW WE DO IT

- Annual scholarships for two children of Airways' staff to attend flying school camps
- Annual funding for one Airways' staff member to complete ATC training
- Support for staff sports teams and events that promote wellness and teamwork

ECONOMIC SUSTAINABILITY

WHAT WE DO

Support the long term viability of the general aviation (GA) community

HOW WE DO IT

- Sponsorship and support for GA organisations, particularly at annual conferences

Supporting the global ATM industry

HOW WE DO IT

- Provide products and training services that help address the global shortage of air traffic controllers

Enhancing aviation safety in the Pacific

HOW WE DO IT

- Provide training, infrastructure support and consultancy to Pacific states to help bring their safety standards in line with New Zealand and other developed countries

Engagement with the crown

REPORTING TO SHAREHOLDING MINISTERS

In compliance with the Act and in accordance with the requirements of the shareholding Ministers, the following reports will be presented to shareholders:

Annual report

Within three months after the end of each financial year, an annual report including:

- audited financial statements for the year
- notes to the financial statements including accounting policies
- a report from the Chair which will include:
  - a review of operations
  - changes in the nature and scope of Airways' activities
  - a summary of achievements measured against performance targets
  - comments on the outlook for the next 12 months
  - statement of dividend payable

Interim report

Within two months of the end of each half-year, an interim report including:

- an abridged, unaudited statement of Airways' financial performance and position
- a qualitative report from the Directors on Airways' performance compared with the objectives set out in the SCI, any significant changes in intent and scope during the half-year and the outlook for the next half-year

Quarterly report

Within one month of the end of each quarter, a quarterly report comprising a commentary and summary of financial statistics indicating performance against targets for the preceding quarter.

Investment project review

Provide a report covering all post-project investment reviews conducted in the previous calendar year greater than $5 million, by 28 February each year.

"No surprises" policy

Inform the Ministers of any material or significant events relating to Airways that may be contentious or could attract public interest.

POLICY FOR SHARE ACQUISITIONS

Any share, equity or asset acquisitions (or sales) will reflect Airways' business strategy requirements for achieving our vision. Airways will consult shareholding Ministers on equity investment or capital expenditure above:

- $10 million on an individual item of capital expenditure or investment in New Zealand
- $5 million investment in an individual overseas project, or other significant investments, even if they do not meet the above thresholds

COMPENSATION FROM THE CROWN

Section 7 of the Act allows the Crown to enter into an agreement with Airways whereby the Crown would pay Airways for undertaking a non-commercial activity. Airways does not currently undertake any such activities but reserves the right to seek payment where Airways is restrained from acting in a normal business-like manner.

THE CROWN'S INVESTMENT IN AIRWAYS

The Directors' estimate of the current commercial value of the Crown's investment in the Airways group as at 30 June 2018 is **$238.2 million** (June 2017 $218.2 million). Key points about the manner in which that value was assessed are:

- The Free cash flow (FCF) to Enterprise methodology was used to calculate the Net Present Value (NPV) of the entire Airways Group, including all subsidiaries, on an after-tax basis.
- The NPV was based on the expected nominal future cash flows set out in the Airways Group's three-year business plan, with forward projections then also made about years four to 10. A terminal value of $216.8 million (present value) was included. A growth rate of 0% per annum was assumed in the terminal value calculation for all business units.
- The discount rate was based on the projected average cost of capital (long-term averages of 7.20% for the core business and 11.02% for the commercial businesses).
- The valuation was prepared by the Airways finance team, and reviewed by Ireland, Wallace & Associates Limited, prior to approval by the Board.
- The current commercial value of the Crown's investment of $238.2 million (the equity value) was calculated by taking the enterprise value of $290.9 million and deducting net debt of $52.7 million.

The valuation compares with a commercial value as at 30 June 2017 of $218.2 million. The key reasons for the increase in commercial value are:

- **Core business** (up $21.5 million): net increases in the capital base used to determine future pricing, with new capital investment of $49.3 million being offset by depreciation of $22.3 million.
- **Commercial businesses** (up $2.7 million): lower risk free rate driving less discounting of future cashflows.
- **Increase in Group net debt** (up $4.2 million): increase in net debt used to fund capital investment.

VALUATION SENSITIVITY AND RANGE	RANGE	LOW	HIGH
Base valuation		**$238.2m**	**$238.2m**
▶ Change in growth factor used in terminal value calculation	0–1%	–	$35.5m
▶ Change in commercial business terminal free cash flow	+/- 10%	($3.1m)	$3.0m
Estimated valuation range		**$235.1m**	**$276.7m**

Appendices

Appendix A:

Accounting policies

A1 BASIS OF PREPARATION

The financial statements are for the consolidated Group ("Airways"), consisting of Airways Corporation of New Zealand Limited and our subsidiaries: Airways International Limited, Airways Training Limited and Aeropath Limited (refer to note C1 for further details). They are prepared in accordance with:

- Generally Accepted Accounting Practice in New Zealand (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 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 financial statements are 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.

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

Airways has adopted the following new standards, interpretations or amendments to existing standards in the 2018/19 financial year.

- NZIFRS 9 (2014), 'Financial Instruments', issued in September 2014 (effective for periods beginning on or after 1 January 2018, with early adoption allowed). Given the relatively simple financial instruments held by the company, management expect the impact of this standard to be largely immaterial. There are however, likely to be small increases in doubtful debt provisions as prospective economic conditions are factored into expected credit losses.
- NZ IFRS 15 (2014), 'Revenue from Contracts with customers', issued in July 2014 (effective for periods beginning on or after 1 January 2017, with early adoption allowed). Management expect this standard to have minimal impact on the timing of revenue recognition for contracts where multiple service components are provided to customers.

The following standard and amendments to existing standards with an impact on Airways have been published and are mandatory for future accounting periods, however Airways has not early adopted them:

- NZIFRS 16 (2016), 'Leases', issued in February 2016 (effective for periods beginning on or after 1 January 2019, with early adoption allowed). Management expects this standard to increase both assets and liabilities on the balance sheet and front load the recognition of lease expenses in the statement of profit and loss to earlier years of lease terms; however, these impacts have not yet been quantified. Airways intends to adopt this standard in the 2020/21 financial year.

A3 PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME INFORMATION

A3.1 Revenue

Airways' principal business is the provision of air traffic management services, however we are also involved in a number of related revenue-generating activities. Airways' revenue streams, and the associated recognition policies, are set out in the table below.

REVENUE TYPE	ACCOUNTING POLICY
▶ Air traffic management	▶ Recognised as flights or other aircraft movements occur
▶ Consulting	▶ Revenue from discrete consultancy services is recognised as our contractual obligations are fulfilled ▶ Revenue from ongoing, recurring consultancy services is recognised as the service is provided
▶ Software licences	▶ Recognised over the life of the licence, or where the licence is perpetual, when the customer has legal title
▶ Training	▶ Recognised as courses are delivered
▶ Publications	▶ Subscription revenue from the publication of aeronautical information is recognised over the period of the subscription (typically one year)

A3.4 Employee entitlements

Superannuation

Airways operates various defined contribution schemes that are funded through fixed contributions into trustee administered funds. Airways has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods. The contributions are recognised as an employee benefit expense in profit or loss when they are due for payment to the funds.

Leave benefits

Liabilities for annual leave, long service leave and retiring leave are accrued and recognised in the balance sheet. These liabilities equal the present value of the estimated future outflows as a result of employee services provided at balance date. Long service leave that has vested with employees is recognised as a current liability within employee entitlements. Actuarial estimates of future demographic trends and employee remuneration are used to calculate the long service leave and retiring leave liabilities that have not yet vested with staff.

A4 INCOME TAX AND RELATED BALANCES

Income tax expense

The tax expense for the year comprises current and deferred tax. Tax is recognised in profit or loss, except to the extent it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is recognised in other comprehensive income or directly in equity, respectively.

Deferred tax is recognised in respect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amount used for taxation purposes. The amount of deferred tax is based on the expected manner of realisation of the carrying amount of assets and liabilities, using tax rates enacted, or substantially enacted at the reporting year-end.

Deferred tax

Deferred tax assets and liabilities are offset on the face of the balance sheet.

A5 FINANCIAL ASSETS AND LIABILITIES

Airways' financial assets and liabilities are classified as either derivatives used for hedging, liabilities at amortised cost or loans and receivables, depending on the purpose for which the transactions were entered into. Management determines the classification at initial recognition and re-evaluates this designation at every reporting date.

Financial liabilities (other than derivatives used for hedging) are recognised initially at fair value, net of any costs incurred, and subsequently measured at amortised cost using the effective interest method. The carrying value of trade and other payables approximates their fair value.

Loans and receivables are recognised initially at fair value, plus any transaction costs, and subsequently measured at amortised cost using the effective interest method, less provision for any impairment. The carrying value of trade and other receivables and cash and cash equivalents approximate their fair value.

Airways uses forward exchange contracts to hedge expenditure and revenue denominated in foreign currency and interest rate swaps to hedge interest repayments on our term debt. The effective portion of changes in the fair value of hedging instruments is recognised in equity until the underlying transaction being hedged occurs. At this point, the value of the hedging instrument is recognised in profit or loss (as interest costs or foreign currency denominated revenue or expenses as appropriate) or on the balance sheet (within the recognised value of any hedged asset or stock purchase). If the hedged transaction is no longer expected to take place, then the cumulative, unrealised balance recognised in equity is recognised immediately in profit or loss.

The derivatives used for hedging are considered level two financial instruments and are recognised on the balance sheet at their fair values, which are determined using observable inputs as follows:

- Forward Exchange Contracts values are determined using observable forward exchange market rates at the balance date.
- Interest Rate Swaps are valued using the "Projected" methodology. For floating rates, this method projects all future floating cash flows and discounts these back to the revaluation date. For fixed rates, the individual cash flows are discounted from the cash flow date to the revaluation date. The discount rate used to calculate the NPV of the deal is the zero coupon curve, based on a blended swaps curve obtained from Reuters.

A6 TRADE AND OTHER RECEIVABLES

Collectability of trade receivables is reviewed on an ongoing basis and uncollectable debts are written off. A provision for doubtful receivables is recognised when there is objective evidence that Airways may not be able to collect some or all amounts due according to the original terms. In determining the expected credit loss, Airways reviews forecast flight volumes as a forward indicator of ability to pay. The amount of the provision will reflect the specific circumstances of individual debtors, however as a guide and based on previous experience:

- debt greater than 90 days but less than one year overdue is discounted by the current cost of capital
- debt greater than one year but less than two years old is discounted by 50% of the carrying value
- debt greater than two years old is discounted by 100% of the carrying value

The amount of the provision is recognised in the statement of profit or loss and other comprehensive income.

A7 TRADE AND OTHER PAYABLES

Trade and other payables are unsecured, non-interest bearing and typically paid within 30 days.

A8 PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLES

Recognition and measurement

All classes of property, plant and equipment and intangibles are initially recorded at cost. Cost is determined by including all charges directly associated with bringing the assets to their location in working condition. Capital work in progress includes expenditure on partially completed assets that management expects will form part of the asset cost at completion.

Where assets are generated internally, costs are only capitalised once a formal investment case has been prepared and approved in line with Airways' delegated financial authority policy. The investment case must demonstrate that:

- the economic and other benefits of the asset are clearly articulated and consistent with Airways' strategy
- the cost associated with the project is within Airways' budget and can be reliably measured
- there are sufficient staffing and technical resources available to complete the project (either internally or externally)
- the asset to be created is technically feasible

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to Airways and the cost of the item can be measured reliably. The carrying amount of any replaced parts is written off.

Depreciation and amortisation

The cost of all fixed and intangible assets (excluding freehold land and work in progress), less their estimated residual value, is written off on a straight line basis over the asset's estimated useful economic life. Asset useful lives and residual values are assessed annually and adjusted if required.

Impairment

All assets are reviewed for potential indicators of impairment at every balance date and whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. For work in progress, these indicators include any changes to the scope or expected outcome of individual projects.

In addition, impairment tests are carried out at every balance date for intangible assets within work in progress regardless of whether indicators of impairment exist.

These tests involve re-assessing the feasibility of the project, the expected cost to completion and the expected economic benefit to be realised. Where the expected economic benefit provided by the asset is lower than the expected cost to completion, the difference is booked as an impairment to the current carrying value in work in progress unless a higher amount could be realised through sale of the asset less costs to sell (fair value less costs to sell). The corresponding impairment is recognised in profit or loss.

C1 GROUP ENTITIES AND OWNERSHIP

Airways Corporation of New Zealand Limited is a limited liability company incorporated and domiciled in New Zealand. The address of our registered office is Level 7, 100 Willis Street, Wellington, New Zealand. We are also a state-owned enterprise established under the State-Owned Enterprise 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.

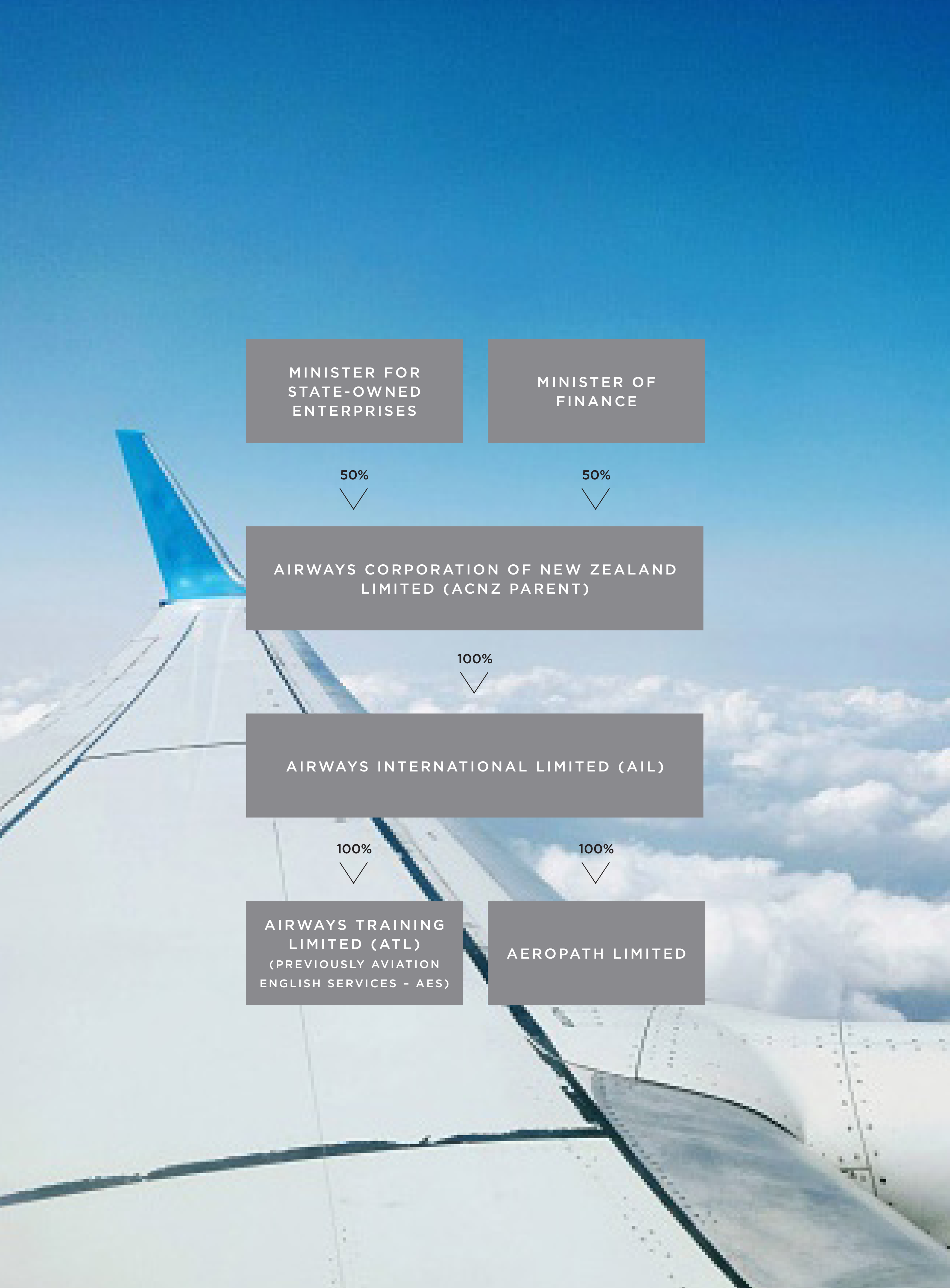
These Group consolidated financial statements are for Airways Corporation of New Zealand Limited (ACNZ) and our subsidiaries: Airways International Limited (AIL); Airways Training Limited (ATL) and Aeropath Limited (Aeropath). "Airways" refers to the Group, and the term "Parent" refers to ACNZ as a separate legal entity.

Subsidiaries are all entities over which Airways has control. Airways controls an entity when it is exposed to, or has rights to, variable returns from our involvement with the entity and has the ability to affect those returns through our power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to Airways and are deconsolidated from the date that control ceases.

Accounting policies of subsidiaries are consistent with the policies adopted by the Parent, and all subsidiaries share a 30 June balance date. The parent recognises its investment in subsidiaries at cost, less impairment.

Key details for each subsidiary in the Group are provided in the table below. All entities are incorporated in New Zealand.

PRINCIPAL ACTIVITY	
Airways International Ltd (AIL)	Aeronautical information management, revenue management, recruitment and training, and air navigation services and maintenance of systems
Aeropath Limited (Aeropath)	Aeronautical information management, publications and procedure design
Airways Training Limited (ATL)	ATC ab initio training and the sale and support of related services and products


MINISTER FOR STATE-OWNED ENTERPRISES
MINISTER OF FINANCE
50%
50%
AIRWAYS CORPORATION OF NEW ZEALAND LIMITED (ACNZ PARENT)
100%
AIRWAYS INTERNATIONAL LIMITED (AIL)
100%
100%
AIRWAYS TRAINING LIMITED (ATL)
(PREVIOUSLY AVIATION ENGLISH SERVICES – AES)
AEROPATH LIMITED

Appendix B:

Financial performance metrics ($NZm)

YEAR ENDED 30 JUNE	ACTUAL FY17	FORECAST FY18	PLAN FY19	PLAN FY20	PLAN FY21
Profitability					
Total revenue	205.1	223.9	235.0	252.9	263.8
EBITDA	55.6	59.4	56.9	70.6	78.8
EBIT	33.4	35.9	33.4	41.9	45.8
NOPAT	23.7	27.1	23.4	29.0	31.2
Shareholders' returns					
Total shareholder return[1]	7.6%	14.2%	–	–	–
Dividend yield	4.2%	4.8%	5.0%	5.5%	5.9%
Dividend payout	33.6%	50.1%	44.0%	44.4%	44.6%
Return on equity	21.9%	21.8%	16.9%	19.1%	18.5%
ROE, adj for IFRS movements and assets revaluations	21.5%	21.5%	16.7%	19.0%	18.4%
Profitability/efficiency					
Return on capital employed	22.4%	21.4%	16.5%	17.0%	16.4%
Return on assets	16.6%	16.3%	13.0%	13.9%	13.6%
Operating margin	27.1%	28.0%	24.1%	27.7%	29.7%
Net profit margin	11.5%	12.7%	9.9%	11.4%	11.8%
Asset turnover	1.0	0.9	0.8	0.8	0.8
Leverage/solvency					
Equity multiplier	1.8	1.8	1.9	2.0	2.0
Gearing ratio (net)	24.5%	25.5%	35.2%	39.9%	38.6%
Interest cover (before capitalised interest)	22.9[2]	21.1	17.8	13.6	15.1
Solvency (current ratio)	0.8	0.8	0.7	0.7	0.7
Growth/investment					
Revenue growth	0.0%	4.8%	5.6%	7.8%	4.5%
EDITDAF growth	1.2%	6.9%	(4.4%)[3]	24.0%	11.7%
NPAT growth	1.9%	14.5%	(13.8%)[3]	24.2%	7.5%
Capital employed growth	10.4%	15.1%	24.6%	19.6%	8.3%
Capital renewal	1.9	2.1	3.1	2.5	1.7

Definitions for the financial performance measures above are at the following link:
https://treasury.govt.nz/sites/default/files/2015-09/fpm-soes.pdf

1. Company valuations are not forecast from 2018–19.
2. Restated to interest cover before capitalised interest.
3. The decrease is a result of the gain on sale of land in 2017–18.

Appendix C:

Core business economic value added (EVA) ($NZm)

BACKGROUND

EVA provides an economic measure of performance and explicitly recognises the expected return to investors. EVA underpins our pricing framework, which is premised on achieving a fair return on the capital invested in the core business, reflected by an EVA result of zero.

Key parameters and inputs into the EVA framework have been presented to our customers through the consultation process for the 2017–2019 pricing round.

EVA	PLAN FY19	PLAN FY20	PLAN FY21
Total capital employed			
Debt employed	159.9	204.0	214.4
Equity employed	139.5	147.4	156.0
	299.4	**351.4**	**370.4**
Charge on operating capital	**17.9**	**23.4**	**26.0**
Economic value added	**(1.0)**	**–**	**–**

COST OF CAPITAL – KEY PARAMETERS			
Risk free rate – 3 year Government Stock	2.64%	2.64%	2.64%
Market risk premium	7.00%	7.00%	7.00%
Business risk factor (asset beta)	0.60	0.60	0.60
WACC range percentile	67th	67th	67th
Cost of capital	**6.92%**	**7.20%**	**7.20%**
Return on capital (RoC)	6.54%	7.20%	7.20%

Directory

BANKERS

ANZ Bank New Zealand Limited

Bank of New Zealand Limited

AUDITORS

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

REGISTERED OFFICE

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

AIRWAYS.CO.NZ

THIS PUBLICATION IS PRINTED USING SUSTAINABLY GROWN PAPERS,
CHEMICAL-FREE PLATING AND PRINTING PROCESSES, AND VEGETABLE-BASED INKS.