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AGL Energy Limited today announced the outcome of its internal and external reviews. The reviews reconfirmed the primary reason for the recent downgrade was that the original guidance was based on “optimistic budget assumptions.” Given the reviews found AGL’s budget and forecasting procedures to be sound, how did the original assumptions come about and what steps have been taken to ensure future assumptions are realistic?

MD & CEO Michael Fraser

Those overly optimistic budget assumptions are behind us. The review confirmed our forecasting systems are sound, and that gives us confidence in our current guidance, which is based on assumptions at the mid point of likely outcomes. I can assure you that future guidance will be based entirely around mid-point assumptions, where there is a 50:50 probability of the outcome being higher or lower.

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As a result of the review AGL has stepped back from its three to five year forecast of EPS growth of 15 percent. To what extent does this reflect a reassessment of the targeted head count reduction and the \$115 million efficiencies assumed in the 15 percent target?

MD & CEO Michael Fraser

On their own Project Phoenix and corporate cost savings could never have delivered 15 percent compound EPS growth for five years. I'd emphasise though that we remain firmly committed to and are on track delivering the benefits of Project Phoenix in line with its business case.

With respect to corporate costs, there have been two key initiatives. One was to right-size our corporate structure post-demerger and we've now largely completed this. The other was to outsource our IT functions and we've progressed this recently with the execution of contracts with both TATA Consultancy Services (TCS) and IBM.

As we take the company forward, rather than one dimensional objectives like head count reductions, we're going to provide guidance around EBITDA and NPAT which is consistent with our focus on delivering overall returns to shareholders.

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You've restated your commitment to AGL's integrated strategy – relating to the development of retail and upstream assets in both gas and electricity markets. To what extent do the previous targets: 5 million customer accounts, 3,000 to 4,000 petajoules of equity gas and 5,000 megawatts of electricity generation capacity, remain appropriate?

MD & CEO Michael Fraser

Our overriding goal is driving shareholder returns, not achieving "set in concrete" customer or upstream targets. Of course customer numbers or the size of our channel to market is important, especially in leveraging the upstream benefits of our integrated strategy and retail economies of scale. But, at the end of the day our main focus will be on margin management. That said a target of 4 to 5 million customers in the medium term is feasible particularly in light of the potential privatisation process in New South Wales.

In terms of equity gas, our modelling suggests a target of around 1,500 to 2,000 petajoules is sensible and achievable over the medium term. We could achieve this through a combination of organic growth from our existing joint ventures and our share in QGC reserves as well as disciplined acquisitions. This is an indicative target; we won't slavishly pursue upstream targets at the expense of everything else. There's often a trade off between acquiring equity gas and EPS growth so that will be one of our considerations. If we can achieve a better outcome by simply contracting for gas then that's what we'll do. Flexibility is key in the dynamic markets in which we operate.

With regard to power generation, we've done considerable work around this and our modelling indicates a medium-term target of 5,000 to 6,000 megawatts across base, intermediate and peaking plant capacity. This is based on our internal customer demand forecasts and would represent around 60 to 70 percent of our own load. This is an appropriate target to achieve the desired portfolio outcomes for the load and customer profile we forecast. Whether it's outright ownership of

the generation asset or operational control will depend on the transaction and what makes most sense from a portfolio benefit and shareholder return perspective.

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AGL's revised net profit guidance for 2008 is \$330 million to \$360 million, equivalent to EPS of 76 to 83 cents. You've also provided EBITDA guidance for 2008 of \$830 million to \$875 million and given one-off guidance for 2009 of EBITDA of \$870 million to \$915 million and NPAT of \$360 million to \$390 million. Why have you added EBITDA to the guidance metrics and what are the key revenue and cost factors that could potentially push earnings to the top or bottom of the range?

CFO Stephen Mikkelsen

One factor would be weather. If we experienced a very mild summer and a very mild winter, clearly our volumes in gas and electricity would be down, which would push our earnings below the mid point. The reverse would be true in a very cold winter and warm summer. Our guidance assumes average temperatures by season based on history.

Similarly, we've had to make assumptions around regulated tariff outcomes and how these impact the revenue streams; variations from our mid-point assumptions could have an impact on the earnings outcome.

Then there are a host of factors unrelated to the underlying business that could influence the NPAT outcome, for example the accounting recognition of tax. This goes to the heart of why we're now providing EBITDA guidance. EBITDA provides a benchmark that excludes those accounting issues and gives the market greater clarity on our expectations of operational outcomes.

In a business like ours, it's more relevant to look at margins rather than revenues and costs in isolation. What we look at is EBITDA growth, which is largely driven by gross margin growth and is a function of both the number of customers and the margin per customer. That's how we're managing the business and that's the guidance we've provided and will continue to provide.

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What has been the trend in retail customer churn and retail prices year to date in your major markets, particularly the Queensland market where retail competition was introduced in July?

MD & CEO Michael Fraser

I don't want to talk specifics at this stage; we'll do that when we announce our interim results in February next year. What I can say though is we're seeing early signs of reduced churn levels but I'd urge against reading any long-term trend into this. Given the focus we've had on Project Phoenix and our retail system improvements I'm comfortable with our customer acquisition and retention performance to date. But I'd reiterate we're not managing the business to customer numbers alone, we're much more focussed on margins.

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Given recent headcount and cost reductions, what ability will you have to maintain monitoring and control of the business?

MD & CEO Michael Fraser

I don't believe the overall headcount is particularly wrong. An important issue though is that we have to re-stock the corporate knowledge base and get the right mix of expertise across the business. There may well need to be additions in some areas, but across the company we're only talking 20 to 30 people and a number of those vacancies are the result of resignations rather than targeted head count reductions.

With respect to monitoring and control of the business, the review has confirmed that our energy risk management systems and practices are working well. This is particularly comforting given our wholesale energy costs add up to around \$3 billion per annum. We've also devoted significant effort around the monitoring and control of Project Phoenix and to date that's working very well with the first 1.2 million customers having successfully migrated to the new system last week.

Considering all these things I'm comfortable we have a very good handle on and are in control of all key aspects of our business.

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AGL attributed part of its earnings downgrade to lower than expected margins in its SME and commercial and industrial books, which were significantly expanded via the \$1.2 billion acquisition of Powerdirect in February. With the extended drought impacting the performance of Southern Hydro, acquired in October 2005, is there now a possibility of substantial impairment charges to AGL's balance sheet relating to Powerdirect and Southern Hydro?

CFO Stephen Mikkelsen

Impairment is a very technical accounting concept. What you need to realise is that it's not tested by individual assets. Rather, assets may well be considered integrated parts of larger cash generating units. Powerdirect and Southern Hydro for example are each integrated parts of different, larger cash generating units. We've reviewed both Powerdirect and Southern Hydro and their wider cash generating units as recently as July and there was no evidence of impairment at that time. We will however, as is standard practice, review cash generating units for impairment in conjunction with our half-year profit reporting process.

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The review found that the risk methodologies underpinning AGL's electricity hedge book were appropriate. The hedge book had a value of \$3.9 billion at the end of June, and AGL previously suggested it had locked in wholesale prices for "90 percent or more" of forecast intra-year load. Given the ongoing strength of wholesale electricity prices, do you see the need to change the current approach to hedging?

MD & CEO Michael Fraser

The opposite. We're essentially hedged for most foreseeable market conditions, in line with our risk policy, at a market competitive cost and our approach has proven to be extremely successful. We've just come through the most tumultuous time in the national electricity market (NEM) since it started; our hedge book performed well and we've continued to provide our customers with cost effective energy. That said, our approach to hedging is one of continuous improvement.

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AGL attributed part of its earnings downgrade to higher wholesale gas costs resulting from the need to secure further gas and gas transportation capacity. What confidence do you now have regarding future supply coverage?

MD & CEO Michael Fraser

We remain confident about the make-up of our wholesale gas book. As we've highlighted in the past, we have substantial contracts in place for the next 10 years. That said, the outlook for winter 2008, particularly in New South Wales, is extremely tight. This is a matter that the industry is currently dealing with and it applies to all market participants, not just us.

We saw some significant demand spikes in winter this year and there are certainly capacity constraints in the New South Wales market. That situation will improve somewhat with the expansion of the Eastern Gas Pipeline and introduction of the QSN interconnect pipeline between Queensland and the southern markets.

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AGL's shares are now trading between \$13.00 and \$13.50, compared with the \$16.50 price of the placement in February that partially funded the Powerdirect acquisition. Will you continue to pursue acquisitions and what balance sheet capacity do you have to do so? Will you actively pursue the New South Wales energy assets that are to be privatised?

MD & CEO Michael Fraser

We'll definitely continue to pursue acquisitions that add value for shareholders. We believe we're well positioned to do that through careful capital management and the potential sale of non-core assets. We recently sold our stake in AlintaAGL for \$520 million, and the sale of our other non-core assets could potentially generate another \$1 billion.

Certainly we'll be looking at the New South Wales energy privatisation, but in a very disciplined way. We have far greater optionality than our competitors in bidding for those assets – we have a very large retail gas presence in New South Wales, so organic growth is a real option if the sale prices get too high. Likewise we may have the option of leveraging existing business partner relationships as part of the New South Wales privatisation process.

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AGL has maintained its 2008 dividend forecast, of a full-year payment of 52 to 55 cents, which implies a payout of about 70 percent. On the current guidance for 2009, your stated policy of a 60 percent payout ratio would imply a dividend of 50 to 54 cents. Can you comment?

CFO Stephen Mikkelsen

Ultimately the dividend will depend on final results for the year and our capital requirements at the time. The 60 percent payout policy is simply a guideline and we have a certain amount of flexibility around that. We've shown this year that where appropriate, we'd go above that payout level.

We believe we can achieve good growth and still maintain what's a solid dividend payout.

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Michael, you took over as managing director in late October. Nearer term, what do you see as your key challenges and what will be your primary areas of focus?

MD & CEO Michael Fraser

Completing this review has been important – we've drawn a line in the sand and can now move forward. My focus is now on four key areas.

Firstly, staff engagement is crucial given the impact of the downgrade and recent events. The wider leadership team and I are putting a lot of work into re-engaging people and improving morale. We have a lot of talented employees and I want to ensure we provide an environment and culture that gives them every opportunity to contribute.

Secondly, our retail business. We're doing a lot of work on improving the level of service our business provides and the successful completion of Project Phoenix is mission critical to giving our people the tools to substantially improve our service performance. We've successfully migrated the first wave of customers to the new systems and we'll be working hard to ensure the smooth migration of the remainder of our customers next year.

Thirdly, the ongoing, disciplined roll-out of our existing integrated strategy. We've made some solid strategic acquisitions recently and announced further renewable development projects. I'm also driving a renewed focus on rigorous capital discipline in every aspect of our strategic delivery.

Finally, we have a market leading position in the renewable space and I intend to ensure we maximise value from this position. The entire market is facing a paradigm shift in a carbon constrained world, we've put a lot of work into preparing for this and I'm confident we'll lead the market. Certainly we see considerable upside for our shareholders.

The business is in good shape, has much embedded optionality and I and the wider team look forward with confidence to delivering ongoing, sustainable benefits for all our stakeholders.

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Thank you Michael and Stephen.

For more information about AGL, visit www.agl.com.au or call Graeme Thompson, Head of Investor Relations, on +61 2 9921 2789

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