Statement of Corporate Intent

2017/18 – 2019/20

AIRWAYS

Contents

Airways New Zealand is a world-leading provider of air traffic management services and a key enabler of the region's aviation system. It is responsible for one of the largest Flight Information Regions in the world at 30 million square kilometres, and manages more than 1 million air traffic movements per year.

Renowned globally for driving innovation and development in the aviation sector, Airways has the expertise, leading-edge thinking, and nimble decision-making to serve the domestic aviation industry and our customers in over 65 countries worldwide.

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Introduction

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 20,550,000 fully paid shares of $1.

ACNZ has four 100% owned subsidiaries – Airways International Limited, Airways Training Limited, Aeropath Limited and Aviation English Services. This Statement of Corporate Intent (SCI) refers to the Airways Group (Airways), including ACNZ and its subsidiaries. It is prepared in accordance with the Act and sets out Airways' business goals and objectives for the period 1 July 2017 to 30 June 2020.

Airways' performance against the objectives outlined in last year's SCI are referred to in the 2016/17 annual report.

AIRWAYS' OBJECTIVES

The principal objective of every SOE, as defined by the Act, is to be a successful business and to:

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

In recognition of these obligations, Airways' overarching vision is to build a progressive airspace environment that enables aviation to thrive, both within New Zealand and around the world. The vision is focused on delivering:

- safe and efficient air traffic management services
- a diversified portfolio of businesses generating growing returns to our shareholder
- upgraded and modernised infrastructure to be an efficient system enabler
- employer of choice offering exciting and diverse career paths to staff.

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Airways' strategic context

Airways' strategic context

Airways provides world-leading air traffic management (ATM) services to the New Zealand and international aviation markets.

The industry in which Airways operates is undergoing a period of unprecedented change. Its traditional business model is based on ground-based radar, centralised control, proprietary systems, specialist skills and sovereign provision – a model that is rapidly transforming in a number of directions. The evolution of satellite-based navigation, decentralised control facilitated by advanced flight deck systems, open systems enabling 'nose-to-tail' internet connectivity on aircraft, automation and the airlines' desire for industry consolidation all bring exciting new developments and challenge. With forecast air passenger traffic growth of 4.7%[1] for Asia Pacific as a whole, the New Zealand aviation industry will need innovative solutions to fund this technological and cultural transition.

Airways prides itself on being one of the world's safest, most efficient and most innovative ATM service providers. We use capability and experience to turn industry change into growth opportunities. In 2012, Airways implemented a new, transformational strategy to take advantage of these industry changes. Our goal was to transform Airways from a traditional, one-dimensional business model into a portfolio of different businesses designed to thrive in the evolving industry.

Following further refinement to the operating model in FY17, the business units that will deliver on this strategy are:

- **System Operator (SO)**: tasked with re-shaping Airways' Air Traffic Control (ATC) into aviation system enablement
- **Commercial business**: autonomous business units, leveraging the organisation's intellectual property to solve customer problems for commercial benefit
- **Corporate Services**: providing 'fit for purpose' advice and support at competitive rates
- **Safety & Assurance**: providing leadership, advice and assurance on safety management/maturity, safety performance and Just Culture to Airways' business units, Executive Leadership Team and Board.

The initial phase of 2012's MANA transformation strategy was focused on enhancing customer focus and creating a portfolio of new commercial businesses. Last year the strategy was refreshed and re-energised through 'Destination 2021' and rolled out across the business. Destination 2021 promotes growth through innovation and simplified business structures while ensuring safety remains fundamental.

The vision of Destination 2021 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.

The five strategic pillars we will focus on over the next five years are:

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 and well-equipped workforce.	Proactively adapt to a rapidly evolving ATM environment, leveraging new technology and industry changes to deliver value to customers.	Utilise data and technology changes to move to an 'electronic way of being', focusing efforts and reducing non-core activities.	Diversifying sources of revenue beyond statutory customers.

[1] Based on IATA long-term forecasts as at October 2016.

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Nature and scope of Airways' business

Nature and scope of Airways' business

SYSTEM OPERATOR

The System Operator (SO)'s primary purpose is to deliver safe, resilient and efficient air traffic management in New Zealand and across the South Pacific. In combining air traffic, technology, data and programme management under one roof, SO offers a total solution for ATM development. SO is defined by a customer-centric approach focussed on performance management, and judged on transparent outcomes.

The System Operator concept expands Airways' role from a traditional, safe separation function to an aviation system enabler, optimising traffic flows across the aviation network.

To deliver on this concept, SO has embarked on a 10-year operational strategy, designed to deliver quantum improvements in the safety, resilience and efficiency of its 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 FY2017/18 include:

- begin the implementation of a new air traffic management platform, replacing the current domestic and oceanic systems
- substantially complete the transition of the first operational team from Christchurch to Auckland
- commence training on a standardised set of operating procedures for combined Terminal operations
- start construction of two new operational facilities in Auckland and Christchurch.

New Zealand's Flight Information Region

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

Core services

System Operator's core business comprises the following key services:

- **Air traffic control services**: This is primarily the separation of aircraft in flight, to standards determined by the appropriate regulatory authority (the Civil Aviation Authority in New Zealand)
- **Air traffic management services**: This is the management of aircraft in flight to maximise access to the most efficient flight paths as determined by the customer, limited only by the constraints of safe delivery of an air traffic management (ATM) service. ATM also includes optimising the flow of aircraft across the aviation network – enabling increased capacity in the network, improved fuel savings, and improved on time performance
- **Navigation services**: These are the navigation infrastructure and supporting services used by aircraft to navigate.

System Operator customers

SO is committed to working with Airways' 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 opportunity 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 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 (using 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.

A key objective for Airways is to improve the maturity and performance of the commercial businesses. Airways assesses maturity using a 13-point framework that covers product, customer demand, market opportunity and growth prospects. This results in an 'Investability Score' that measures business maturity and the relative appeal of the business to external investment. Airways aims to progress its commercial businesses through the stage gates defined below, creating both shareholder value and investment options.

Earn the right to exist

- Incubate within Airways structures
- Introduce incentive-based employment terms and conditions
- Achieve investable score > 40

Earn the right to grow

- Office premises off Airways campus considered
- Dedicated legal structure once scale reached, defined as:
  - investable score > 50
  - NOPAT > $2m
  - External revenues > 80%

Earn the right to divest

- Evaluate options to;
  - Divest – exit strategy, or
  - Invest – accelerate growth

COMMERCIAL PRODUCTS AND SERVICES

The commercial portfolio currently comprises three businesses, each at varying levels of maturity and autonomy. The three businesses, and their product and service offerings, are set out below:

Training

- Domestic campuses supporting New Zealand-based ATC training for international ANSPs
- International campuses, run in conjunction with in-country partners
- An online training platform (Aviation Knowledge Online or "AKO")

Aviation Services

- Upper airspace ATM services to Pacific ANSPs
- ATM and aviation-related consultancy, equipment installation and maintenance services
- Flight-Yield, a modularised revenue management solution offering generation of simple billing data through to a full, revenue bureau service

Aeropath

- Next generation aeronautical information management
- Procedure design and maintenance services across the Asia Pacific Region

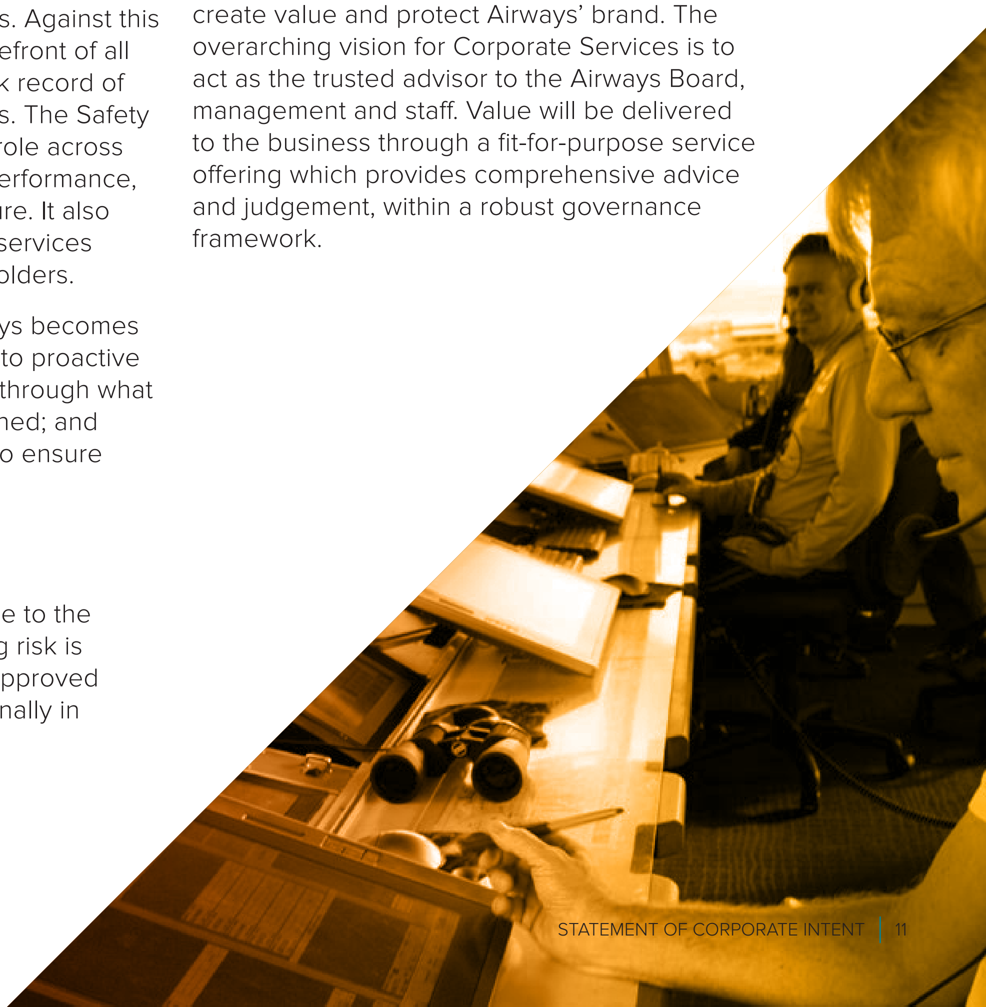
SAFETY & ASSURANCE

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 it does and has established a proven track record of excellent safety results amoungst its 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 will ensure that Airways becomes 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, working transversally 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 will be delivered to the business through a fit-for-purpose service offering which provides comprehensive advice and judgement, within a robust governance framework.



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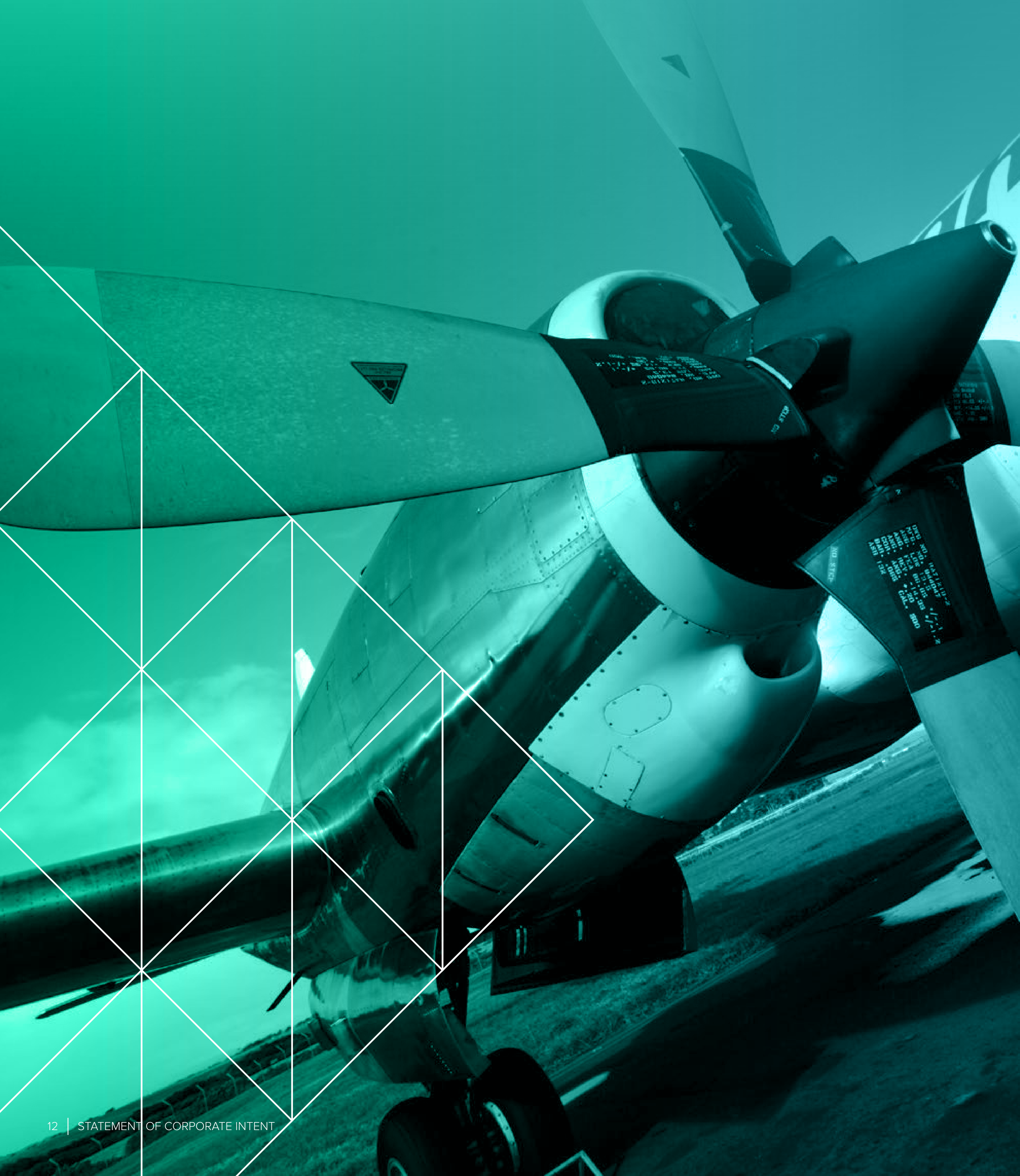
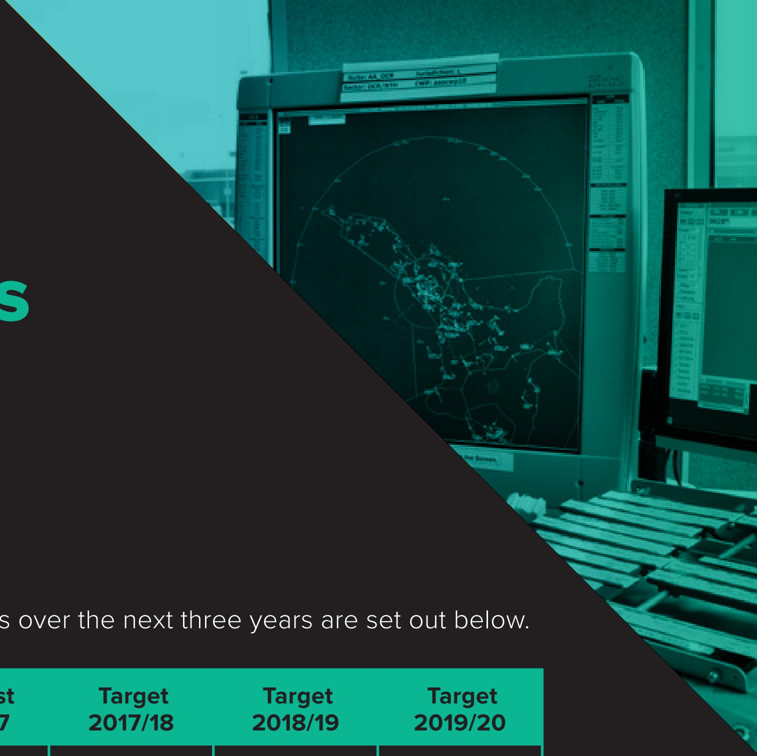
Performance targets and measures



Performance targets and measures



KEY MEASURES OF SUCCESS

The key business, financial and leadership targets for business over the next three years are set out below.

Business	Forecast 2016/17	Target 2017/18	Target 2018/19	Target 2019/20
Near collision events	Nil	Nil	Nil	Nil
Serious harm injuries	Nil	Nil	Nil	Nil
System availability	99.98%	99.95%	99.95%	99.95%
Customer satisfaction in customer survey	87%	FY17 + 2%	FY18 + 2%	FY19 + 2%
Financial				
Group NOPAT	$24.00m	$26.95m[1]	$26.08m	$27.14m
Capex – value creating investments	$41.70m	$45.49m	$48.13m	$47.99m
Return on capital (statutory business)	10.59%	8.08%	7.78%	7.17%
Commercial business NOPAT	$4.80m	$8.52m	$9.34m	$10.27m
Leadership				
Staff engagement	71%	FY17 + 2%	FY18 + 2%	FY19 + 2%
Succession (suitable candidates for senior roles)	3	≥3	≥3	≥3
Visibility – internal event platforms (per week)	2	≥2	≥2	≥2

[1] Includes a $3.3m one-off gain on sale of land.

KEY STRATEGIC INITIATIVES

The key strategies to be employed by each business unit during 2017/18 are set out in the first section of this document. The key initiatives that will enable the business to deliver on those strategies are set out below:

System Operator	Commercial businesses
• Enhance safety training • Enhance cyber security • Progress the Operational Strategy • Implement the new ATM system • Develop innovative enhancements to the broader ATM service offering • Establish a robust business intelligence (BI) capability.	• **Training**: grow external revenue through offshore expansion and *air*Books • **Aviation Services**: focus sales strategy on capturing market share in A ustralia and South East Asia • **Aeropath**: build external revenue base through new products and partnerships • Leverage new partnerships, sales channels and products to diversify revenue streams.
Corporate Services	**Safety & Assurance**
• Leverage strategic partnerships to deliver Destination 2021 • Develop and roll out an enhanced employee relations and workplace culture strategy • Progress the Property Strategy • Deliver continuous improvement in core services, systems and processes.	• Develop the Barrier Model to enhance understanding of contributing factors in safety events • Embed Safety by Design • Integrate Human Factors into the Safety Management System • Implement the Security Smart Programme.

FINANCIAL FORECASTS ($NZM)

Airways is on target to deliver a positive full-year result of Group NOPAT of $24.0 million for 2016/17, ahead of budget ($18.1 million) and the strong performance in the prior year ($23.2 million).

Statutory Services' full year NOPAT is forecast to be $19.2 million against a budget of $10.7 million. NOPAT has benefited from continued strengthening in air traffic volumes (over and above the growth forecasted as part of the FY17–19 pricing consultation) and sound cost management in respect of discretionary spend.

Commercial businesses' full-year NOPAT is expected to be $4.8 million versus a budget of $7.4 million. The main variance is the result of a slow uptake of the Flight-Yield service and temporary delays in realising the benefits of a restructure implemented at the end of 2015/16.

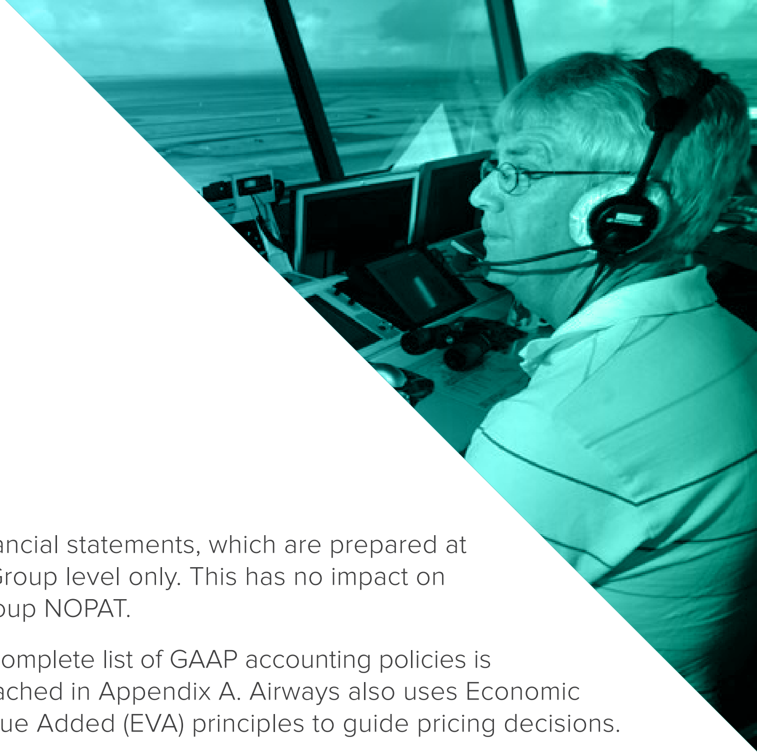
Overall the forecast result, while below budget, reflects continued positive growth, and a 37% improvement on the $3.5m NOPAT recorded in the prior year.

Airways is forecasting to invest $41.7 million in service improvement (capital) projects for 2016/17, in line with budget and $6.3 million higher than the prior year. The current year has seen both the launch of a number of significant new investments – including a new ATM platform and satellite enabled surveillance network – as well as significant progress on a new, landmark control tower at Wellington Airport.

Revenue, NOPAT and other key financial indicators for 2016/17 to 2019/20 are set out below:

$m	Forecast 2016/17	Target 2017/18	Target 2018/19	Target 2019/20
Revenue (includes internal revenue)				
Statutory Services	185.05	189.59	196.91	200.70
Commercial businesses	38.41	47.94	52.12	57.16
GROUP REVENUE	**223.46**	**237.53**	**249.03**	**257.86**
NOPAT				
Statutory Services	19.20	18.43	16.74	16.87
Commercial businesses	4.80	8.52	9.34	10.27
GROUP NOPAT	**24.00**	**26.95**	**26.08**	**27.14**

Key financial indicators				
Headcount (FTEs)	775.4	779.8	786.7	794.7
Dividends ($m)	9.0	11.0	12.0	13.0



Airways prepares Financial Statements in accordance with Generally Accepted Accounting Principles (GAAP). The GAAP 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 the following matter. Revenue is determined at the individual business unit level and 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.

A complete list of GAAP accounting policies is attached in Appendix A. Airways also uses Economic Value Added (EVA) principles to guide pricing decisions.

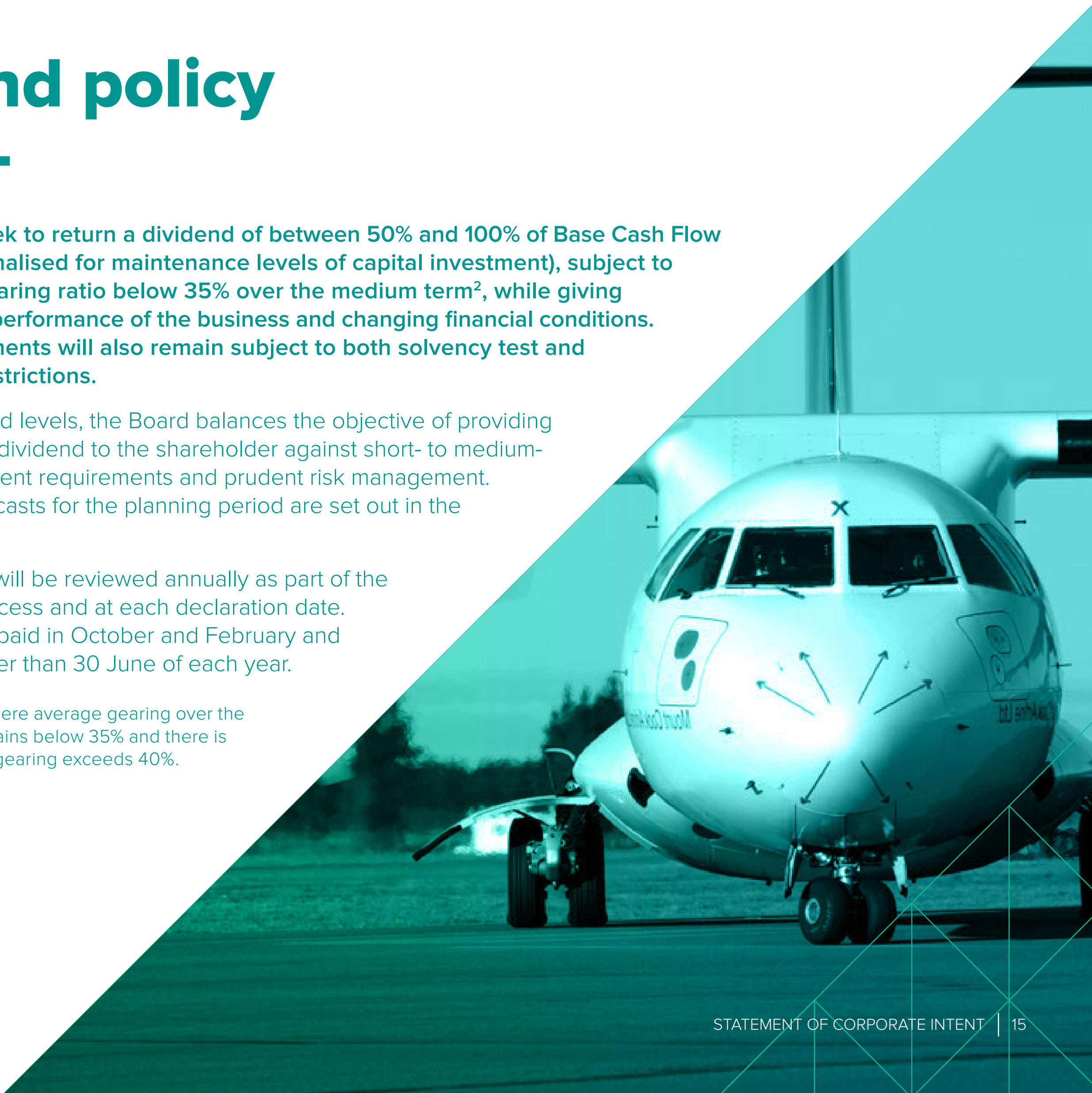
Dividend policy

The Directors will seek to return a dividend of between 50% and 100% of Base 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[2], 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 balances the objective of providing a stable or increasing dividend to the shareholder against short- to medium-term business investment requirements and prudent risk management. Specific dividend forecasts for the planning period are set out in the table opposite.

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.

[2] 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%.



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Corporate and social responsibility

Corporate and social responsibility

Airways' corporate and social responsibility objectives are to provide a safe, cost effective and environmentally friendly air navigation service within New Zealand's airspace. Airways will focus on the below key areas in 2017/18:

SAFETY

Safety underpins all activity at Airways. Airways works with its customers to guide aircraft and their passengers to their destination safely and efficiently. The health and safety of Airways' staff is a key focus. Airways takes significant lead roles on the global trade association CANSO's Executive Committee, its Safety Standing Committee and Safety Sub-Committee, and New Zealand's Business Leaders Health and Safety Forum. Airways partners in an annual aviation safety scholarship in memory of air traffic controller Jilly Murphy who passed away in the Canterbury earthquake of 22 February 2011.

CARBON EMISSIONS

Airways plays a leading role with airline customers in reducing New Zealand's aviation greenhouse gas emissions. To this end Airways has a number of important programmes which will assist the airlines to fly the most direct routes with a minimum of delay, hence reducing fuel consumption and emissions. Airways estimates it will provide $15.4 million of fuel savings in 2017 (against usage prior to the introduction of these programmes), and with it large CO_2 emission reductions, in line with savings in the previous year. Similar savings are expected in 2017/18. Airways also chairs the Asia and Pacific Initiative to Reduce Emissions (ASPIRE).

AVIATION INDUSTRY SUPPORT

Airways plays a critical, aviation system enabler role in the New Zealand economy. It supports aviation's pivotal position in tourism, transport and exporting through the provision of safe, resilient and increasingly efficient airspace management. While Airways largely operates 'below the radar', it has a responsibility to deliver service reliability and continuity of service in a safe manner to support New Zealand Inc. and the Airways brand. Airways offers an annual scholarship for a young person to attend the Walsh flying school in Matamata, called the Glenn C Ashton Memorial Scholarship, in memory of an air traffic controller who passed away in 2000. As part of Airways' support of the general aviation community, the company also sponsors a number of regional and national events.

GROWTH

Airways has a track record of innovation and is recognised globally as an industry leader. Airways plans to grow through commercialising its intellectual property, creating high quality jobs for New Zealanders and enhancing shareholder value.

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Reporting to shareholding Ministers

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.

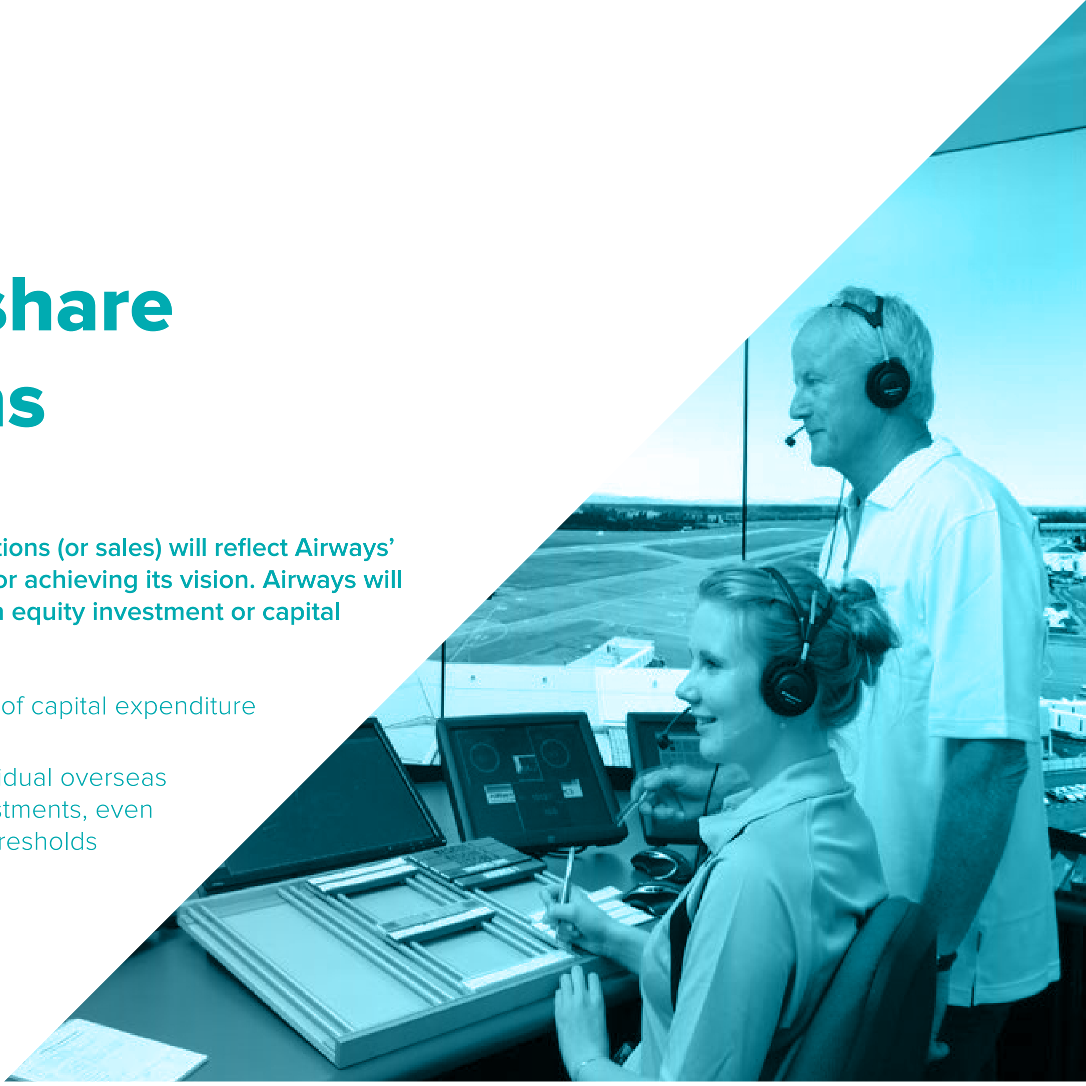
INVESTMENT PROJECT REVIEW

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

Policy for share acquisitions

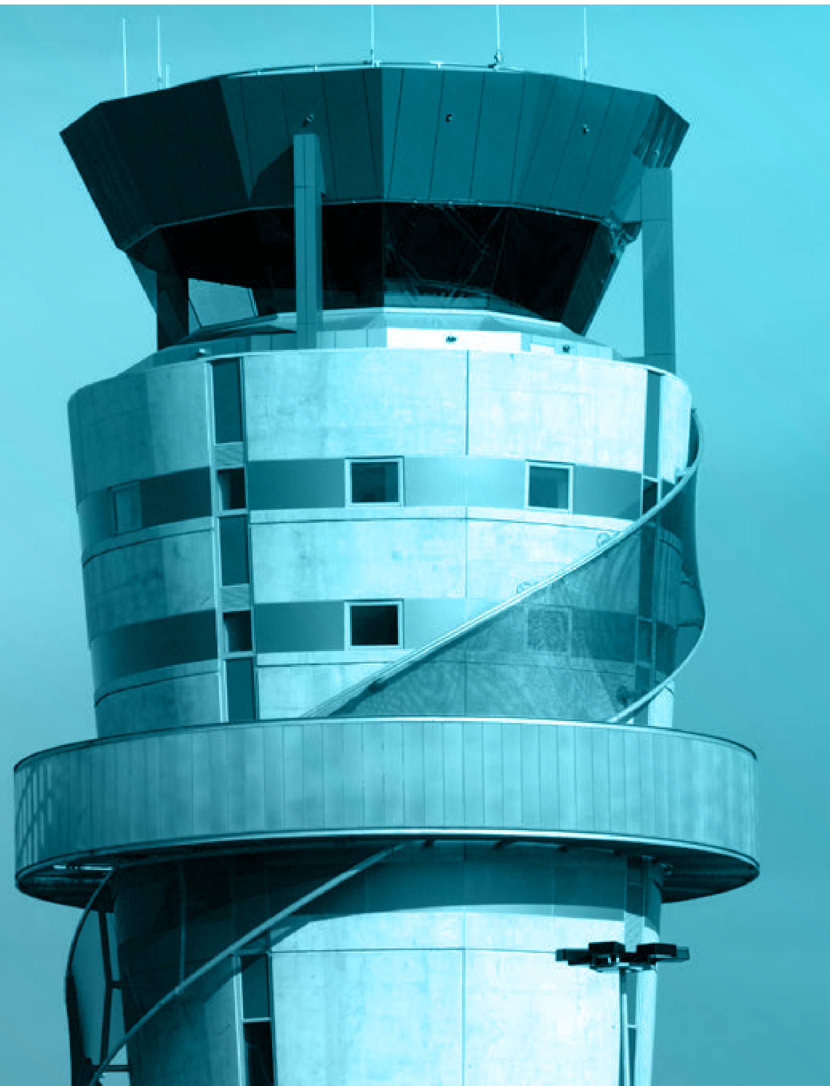
Any share, equity or asset acquisitions (or sales) will reflect Airways' business strategy requirements for achieving its vision. Airways will consult shareholding Ministers on equity investment or capital expenditure above:

- $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 for 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 2017 is $218.2 million (June 2016 $211.2 million). Key points about the manner in which that value was assessed are:

- the FCF (Free Cash Flow) 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 4 to 10. A terminal value of $181.6 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 7.17% for the System Operator business and 11.34% for the commercial businesses)
- the valuation was prepared by the Airways finance team, and reviewed by Ireland, Wallace & Associates Limited, before approval by the Board
- the current commercial value of the Crown's investment of $218.2 million (the equity value) was calculated by taking the enterprise value of $266.7 million and deducting net debt of $48.5 million.

The valuation compares with a commercial value as at 30 June 2016 of $211.2 million. The key reasons for the increase in commercial value are:

- **System Operator – Statutory Services** (up $11.3 million): new capital investment of $41.7 million, offset by depreciation and a reduction in working capital requirements
- **Commercial businesses** (up $1.8 million): higher projected cashflows following a recent restructure of governance and overhead functions, offset by an increase in risk-free rates and a standardisation of asset betas across the portfolio
- **Increase in Group net debt** (up $6.1 million): increase in net debt as cash on hand is used to fund required capital investment, offset by a decrease in implied debt from capitalised property leases

Valuation sensitivity and range	Range	Low	High
Base valuation		**$218.2m**	**$218.2m**
Change in growth factor used in terminal value calculation	0%–1%	-	$29.7m
Change in commercial business terminal free cash flow	+/- 10%	($3.4m)	$3.4m
Estimated valuation range		**$214.8m**	**$251.3m**

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 its subsidiaries: Airways International Limited, Airways Training Limited and Aviation English Services (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 not adopted any new standards, interpretations or amendments to existing standards in the current financial year. The following standards 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:

- 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 some impact on the timing of revenue recognition for contracts where multiple service components are provided to customers, however this impact has not yet been quantified. Airways intends to adopt this standard in the 2018/19 financial year.
- NZ IFRS 16 (2016), 'Leases', issued in February 2016 (effective for periods beginning on or after 1 January 2019, with early adoption allowed). Management expect 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, it is 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 based on the percentage of expected project time and material costs completed, using the expected project margin Revenue from ongoing, recurring consultancy services is recognised as the service is provided
Training	Recognised as courses are delivered

A3.4 EMPLOYEE ENTITLEMENTS

Superannuation

Airways operates various defined contribution schemes which 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 when they are due.

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 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 and cash and cash equivalents 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 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 its 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 2 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.

Appendix A: Accounting policies (Continued)

A6 TRADE AND OTHER RECEIVABLES

Collectability of trade receivables is reviewed on an ongoing basis and uncollectible 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. The amount of the provision will reflect the specific circumstances of individual debtors, including the expected ability and intent to pay. However, as a guide and based on previous experience:

- debt which is greater than 90 days but less than one year overdue is discounted by the current cost of capital;
- debt which is greater than one year but less than two years old is discounted by 50% of the carrying value; and
- debt which is 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;
- there are sufficient staffing and technical resources available to complete the project (either internally or externally); and
- 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

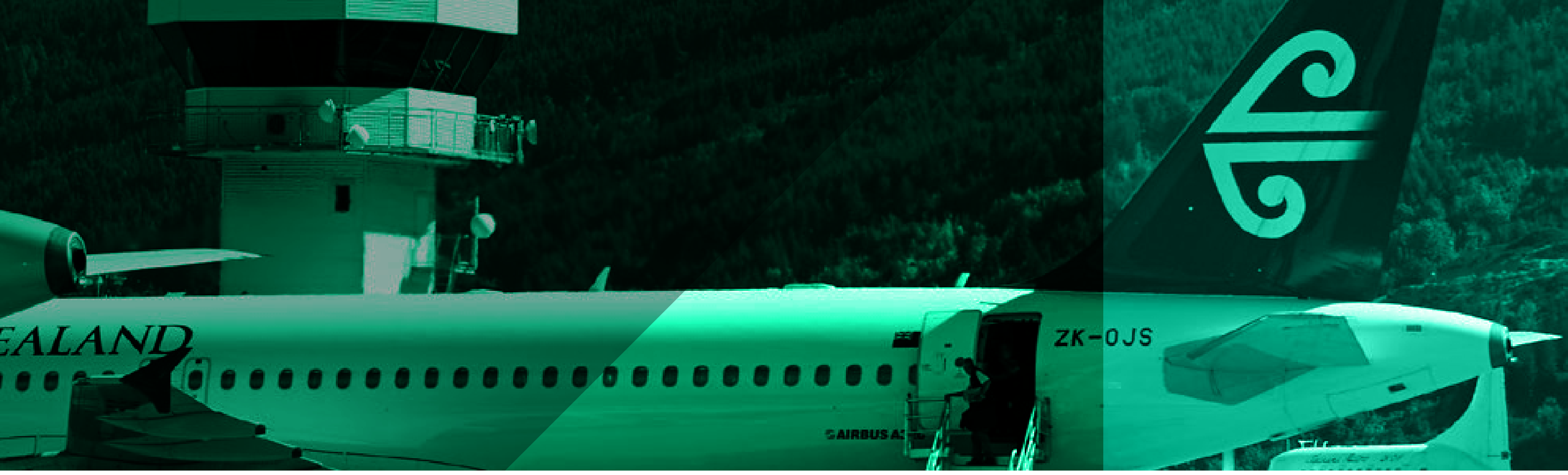
The cost of all fixed and intangible assets (excluding freehold land and work in progress), less their estimated residual value, is written off on a straight line basis over the asset's estimated useful economic life. Asset useful lives and residual values are assessed annually and adjusted if required.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

Land	not depreciated
Buildings structure:	
Freehold	10–40 years
Leasehold	8–40 years
Plant and equipment	3–30 years
Computer equipment	3–20 years
Furniture and fittings	5–25 years
Motor vehicles	3–10 years
Intangibles	2–10 years
Capital work in progress	not depreciated

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.

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 its registered office is Level 7, 100 Willis Street, Wellington, New Zealand. It is 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 its subsidiaries: Airways International Limited (AIL); Airways Training Limited (ATL); Aeropath Limited (Aeropath) and Aviation English Services (AES). "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 its involvement with the entity and has the ability to affect those returns through its 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)	Holding company
Aviation English Services (AES)	Aviation English training

ACNZ (Parent)

100% AIRWAYS TRAINING LTD (ATL)

100% AVIATION ENGLISH SERVICES (AES)

100% AIRWAYS INTERNATIONAL LTD (AIL)

100% AEROPATH LTD (AEROPATH)

Previously 80% owned and equity accounted

C2 JOINT ARRANGEMENTS AND OTHER INVESTMENTS

Investments in joint arrangements are classified as either joint operations or joint ventures, depending on the contractual rights and obligations of each investor. Joint ventures are accounted for using the equity method, whereas investments in joint operations are reflected through the recognition of Airways' portion of assets, liabilities, revenues and expenses incurred.

Appendix B: Financial performance metrics ($NZm)

Year ended 30 June	Actual 2015/16	Forecast 2016/17	Target 2017/18	Target 2018/19	Target 2019/20
Profitability					
Total revenue	205.13	223.46	237.53	249.03	257.86
EBITDA	54.94	56.79	61.04	61.74	64.76
EBIT	33.59	34.49	37.44	37.19	38.46
NOPAT	23.23	24.00	26.95	26.08	27.14
Shareholders' returns					
Total shareholder return[1]	23.9%	7.6%	-	-	-
Dividend yield	4.6%	4.2%	5.0%	5.5%	6.0%
Dividend payout	36.2%	33.3%	43.2%	39.4%	42.3%
Return on equity	24.5%	22.0%	21.9%	18.9%	17.8%
ROE, adj for IFRS movements and assets revaluations	24.3%	22.0%	21.9%	18.9%	17.8%
Profitability/efficiency					
Return on capital employed	25.2%	23.1%	22.3%	19.6%	18.1%
Return on assets	18.2%	17.1%	17.0%	15.3%	14.4%
Operating margin	26.8%	26.3%	26.4%	25.5%	25.8%
Net profit margin	11.3%	11.1%	11.7%	10.7%	10.8%
Asset turnover	1.1	1.0	1.0	0.9	0.9
Leverage/solvency					
Equity multiplier	1.9	1.8	1.8	1.8	1.8
Gearing ratio (net)	27.2%	25.9%	25.4%	26.9%	27.5%
Interest cover	22.2	49.3	47.2	63.2	85.1
Solvency (current ratio)	0.9	0.8	0.9	0.9	0.9
Growth/investment					
Revenue growth	10.1%	5.4%	6.9%	5.0%	3.6%
EDITDAF growth	25.2%	3.4%	7.5%	1.1%	4.9%
NPAT growth	53.8%	3.3%	12.3%	(3.2%)	4.1%
Capital employed growth	13.8%	11.0%	13.3%	12.9%	11.0%
Capital renewal	1.7	1.9	1.9	2.0	1.8

Definitions for the financial performance measures above can be found at the following link:
http://www.treasury.govt.nz/statesector/commercial/guidance/fpm-soes.pdf

[1] Company valuations are not forecast from 2017/18.

Appendix C: Summary of EVA performance

BACKGROUND

EVA provides an economic measure of performance and explicitly recognises the expected return to investors. EVA underpins our statutory business pricing framework, which is premised on achieving a fair return on the capital invested in the regulated business (Statutory Services), 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 2017–19 pricing round.

The summary EVA metrics outlined below are for the System Operator – Statutory Services business only.

EVA TARGETS

Statutory Services – EVA ($m)	Forecast 2016/17	Target 2017/18	Target 2018/19	Target 2019/20
Total Capital Employed				
Debt employed	68.78	81.94	110.01	132.98
Equity employed	125.88	131.35	136.43	140.32
	194.66	**213.29**	**246.44**	**273.30**
Charge On Operating Capital	**13.24**	**14.62**	**16.47**	**18.62**
Economic Value Added	**7.04**	**1.87**	**1.42**	**-**
Return on capital (RoC)	**10.59%**	**8.08%**	**7.78%**	**7.17%**
Cost of Capital – key parameters				
Risk free rate – three-year Government stock	2.31%	2.66%	2.66%	2.66%
Market risk premium	7.0%	7.0%	7.0%	7.0%
Business risk factor (asset beta)	0.60	0.60	0.60	0.60
WACC range percentile	67^{th}	67^{th}	67^{th}	67^{th}
Cost of Capital	**6.92%**	**7.17%**	**7.17%**	**7.17%**

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