

SNOWY HYDRO LIMITED

STATEMENT OF CORPORATE INTENT 2014

1. INTRODUCTION

This Statement of Corporate Intent 2014 for Snowy Hydro Limited (“**Snowy Hydro**” or the “**Company**”) continues a focus on the continued development and augmentation of Snowy Hydro’s current and successful business model as a major wholesaler of electricity price risk management products in the National Electricity Market (“**NEM**”).

The strength of this business model is derived from the Company’s sustainable competitive advantage in the development of innovative electricity price risk management hedging products in combination with the Snowy Scheme’s substantial intra- and inter-year hydro energy storage capability, which is without equal in the NEM, the location advantages of its positioning between the major Victorian and NSW NEM energy end-users, and the Company’s large capacity and highly flexible start/stop hydro and gas generation capability.

In continuing to develop and augment its business model, Snowy Hydro aims to optimise the balance between maximising returns and managing financial risk exposure, while complying with its water release obligations under the *Snowy Water Licence* and minimising operational risk.

Snowy Hydro will continue to target growth and development areas that relate most directly either to developing its competitive advantages or reducing its risk exposures. Reducing risk exposures means addressing gas resource risk, transmission risk, wholesale contract renewal risk and liquidity (financing) risk.

2. VISION, MISSION AND GOALS

2.1 Corporate Vision and Mission

Snowy Hydro’s corporate vision is:

“To be the industry leader in the provision of price and supply risk management products in the National Electricity Market and of other products that manage risk in related markets including water and environment.”

Snowy Hydro’s corporate mission is:

“To deliver superior financial returns by being the preferred supplier of risk management products, developing our people, utilising and developing our water resources, physical assets and dual fuel capabilities, and exceeding customer and stakeholder expectations while demonstrating best practice in safety and health, asset and environmental management.”

2.2 Be the Industry Leader

Snowy Hydro aims, at a minimum, to maintain its position as the industry leader in the NEM in providing electricity risk management products and aims to operate a profitable and sustainable electricity retail business.

2.3 Provide Superior and Secure Returns

The operation of the Snowy Scheme is subject to regulation for matters including the environment and, in particular, western river water releases and environmental flow obligations.

In exercising its water rights and complying with its water obligations, Snowy Hydro seeks to provide superior and secure returns from generation activities, from the sale of electricity price risk management products and the sale of products relating to the timing of Snowy Scheme water releases.

Snowy Hydro will actively pursue a growth strategy to maximise shareholder value while managing financial and operating risk and fulfilling its obligations to all stakeholders.

2.4 Develop Asset Base

Consistent with this aim and to protect shareholder value and enhance existing operations, it is a priority to develop the Company's current asset base, business skills and operational capabilities.

2.5 Maintain Relevance to Customers

Maintaining the Company's relevance to customers (that is, the ability to service their growth) will require a commensurate increase in Snowy Hydro's scale. In the absence of at least maintaining its current scale and capabilities relative to the market, it is reasonable to expect that competitors (and customers) would fill this void and that this will result in a significant diminution in shareholder value over time.

Accordingly, to further reduce the overall risk exposure of the Company and respond to the business strategies of its competitors, Snowy Hydro will consider further opportunities in relation to gas-fired generation investments, environmental and water related products, and to grow its directly contracted energy end-use customers, including commercial and industrial ('C&I') and mass market.

2.6 Best Practice Operator of Plant

Snowy Hydro aims to be recognised internationally as a best-practice operator of hydro-electric and gas-fired power generation assets and to be well regarded in the communities in which it operates.

At all times, the Company ensures maximising its commercial value is consistent with meeting its western river and environmental water release obligations under the *Snowy Water Licence*.

2.7 People and Culture

A key part of Snowy Hydro's strategy to deliver sustainable competitive advantage and underpin growth in shareholder value is the Company's ability to attract, retain and

develop superior performers and continue to improve upon the organisation's excellent environmental and safety performance.

Innovation and flexibility by both individuals and work teams is required, valued and rewarded as a means of continuing to build a high performance culture.

High levels of safety and environmental performance and demonstrated corporate social responsibility is integral to demonstrating ethical leadership and maintaining a performance culture.

2.8 Achieving Those Goals

To achieve these goals, Snowy Hydro has actively adopted innovative programmes covering:

- (1) Clean, Green and Safe (corporate wide focus);
- (2) Behaviour based safety programmes;
- (3) Continuous Improvement (team focus);
- (4) Best practice visits other organisations;
- (5) Identification of "model" markets and "model" companies;
- (6) ISO9000 Certification (quality systems);
- (7) ISO14000 Certification (environmental and safety systems);
- (8) Goals, Actions, Measures performance appraisal (individual focus);
- (9) Company wide incentives/ rewards programme;
- (10) Learning organisation and knowledge transfer programmes;
- (11) 360 degree performance review and personal growth programmes; and
- (12) Focus on "Economic Value Added".

2.9 Core Values Underpinning Corporate Culture

The core values underpinning Snowy Hydro's corporate culture are:

RESPECT FOR PEOPLE	<ol style="list-style-type: none"> (a) Put safety first. (b) Encourage participation. (c) Facilitate communication. (d) Promote individual and team development. (e) Recognise success.
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PRODUCT INNOVATION	<ul style="list-style-type: none"> (a) Exploit uncertainty. (b) Create opportunities. (c) Foster product evolution. (d) Leverage off policy and regulatory changes.
SHAREHOLDER VALUE	<ul style="list-style-type: none"> (a) Think like an owner. (b) Create value adding initiatives. (c) Use capital wisely. (d) Reward value creation.
CUSTOMER RESPONSIVENESS	<ul style="list-style-type: none"> (a) "Delight" the customer. (b) Anticipate needs. (c) Create "partnerships". (d) Also apply these principles to internal dealings.
ENVIRONMENTAL SENSITIVITY	<ul style="list-style-type: none"> (a) Satisfy the "spirit". (b) Demonstrate leadership. (c) Promote initiatives.
MINIMISE NON VALUE ADDING ACTIVITY	<ul style="list-style-type: none"> (a) Eliminate waste. (b) Maintain constancy of purpose. (c) Simplify. (d) Manage with facts.
CONTINUOUS IMPROVEMENT	<ul style="list-style-type: none"> (a) Do it better each time. (b) Deal with causes not symptoms. (c) Apply best practice in all we do. (d) Provide compelling justification for spending.

3. SCOPE OF OPERATIONS

3.1 The Snowy Scheme and Gas Fired Generation Plant

Snowy Hydro owns and operates the Snowy Mountains Hydro-electric Scheme ("**Snowy Scheme**"). The hydro-electric assets of the Snowy Scheme, along with gas-fired peaking plant, are operated as an integrated portfolio of production assets. These, together with energy retailing operations, form the core of the Snowy Hydro business.

The Company seeks to ensure the reliability and integrity of its physical assets to enable the Company to continue to underwrite and drive its commercial returns from participation in the NEM and to comply with its water release obligations under the *Snowy Water Licence*.

The Snowy Scheme's integrated system of 16 large dams, 7 major tunnels and 8

separate generating/pumping facilities are located predominantly in the Kosciuszko National Park (“**KNP**”). Total hydro-electric generation capacity is currently at about 3,900 MW. Historical energy production has averaged 4,975GWh per annum and water releases have averaged 2,328 GL per annum. The Snowy Scheme also has approximately 680 MW of pumping capacity.

Snowy Hydro also owns and operates open cycle gas-fired generating facilities located in Victoria, in the Latrobe Valley (300MW) and at Laverton (320MW).

All of Snowy Hydro’s generating plant is operated from Cooma and is managed as an integrated portfolio of production assets irrespective of the nature of the “fuel”.

Snowy Hydro will continue to increase its generating capacity through low-cost, value-accretive incremental upgrades to the Company’s existing hydro-electric and gas-fired generating assets.

Snowy Hydro’s contracts, finance, legal, marketing and trading groups and associated support functions are located in the Sydney central business district.

3.2 Snowy Hydro and the NEM

Snowy Hydro is a registered generator in the National Electricity Market (“**NEM**”), being the five-State inter-connected power system comprising Queensland, New South Wales, Victoria, Tasmania and South Australia.

Snowy Hydro is the seventh-largest NEM generator by installed capacity and trades all of its electrical energy into the NEM power pool. Snowy Hydro is the premier supplier of electricity price risk management products and electrical ancillary services, such as “black start capacity” and reactive power, in the NEM. Snowy Hydro is also the largest single supplier of renewable energy in the mainland NEM.

3.3 Snowy Hydro’s Risk Management Product Offerings

Unlike base load generators, Snowy Hydro derives much of its value from risk management of uncertainty and volatility in the NEM. The fast start and flexible operating capability of its hydro and gas-fired power generation assets enables Snowy Hydro to manage electricity market risks and to offer a broad range of electricity price risk management products to other electricity market participants.

Similarly, but to a lesser extent, Snowy Hydro offers water supply reliability risk management products to water users in the Murray and Murrumbidgee valleys.

Snowy Hydro’s electricity and water products are continually evolving to meet changing customer needs.

Snowy Hydro aims increase its sales of risk management products whilst maintaining an overall risk exposure that secures optimal financial returns for the risk accepted. Consistent with this strategy, Snowy Hydro will continue to assess opportunities for the acquisition and establishment of additional generating capacity in the NEM and to progress such investments as and when they add to shareholder value. Snowy Hydro intends to, at a minimum, maintain its share of the peaking energy market.

Through the provision of ancillary and other specialised products and services, Snowy Hydro will continue to play a key role in maintaining the operational security of the

interconnected five-State power system. Snowy Hydro will work with transmission asset owners and regulators to implement incentive regimes to ensure that the operations of the transmission assets remain consistent with Snowy Hydro's market and system-support activities.

3.4 Snowy Hydro's Energy Retail Operations

Snowy Hydro has a growing electricity retailing business located in Victoria, trading as Red Energy. The majority of Red's customers are in Victoria, comprising both gas and electricity products, together with small customer bases in South Australia and NSW where only electricity products are offered. Red Energy also has retail licences for the Australian Capital Territory and Queensland, however is not currently active in those States.

3.5 Snowy Hydro's Obligations Under the *Snowy Water Licence*

An Annual Water Operating Plan, approved by the NSW Water Administration Ministerial Corporation, defines Snowy Hydro's water release obligations for each water year.

4. RETURNS TO SHAREHOLDERS

4.1 Dividends and Dividend Policy

Snowy Hydro's dividend policy is to distribute surplus cash, twice annually, but only after considering the business outlook, capital expenditure commitments, growth opportunities and the need to maintain a strong investment grade credit rating thus making allowances for the investment necessary to maintain the business assets and enable the company to remain competitive in the market place.

For planning purposes, it is considered that a dividend payout ratio to a five year average of 70 per cent or more of NPAT is a suitable dividend payment target. Three year forward forecasts will be provided annually to shareholders on a "best endeavours" basis. Such forecasts will be reviewed bi-annually. In each financial year, the Board will inform shareholders of the proposed dividend payment and payout ratio.

Actual dividend payments are approved by the Board having regard to the financial parameters noted above, and after consultation with shareholders. It is acknowledged that shareholders have a preference for dividends over capital growth while noting that the shareholders' key priorities are to maintain:

- (1) the long-term viability of the business;
- (2) a stable and reliable dividend stream;
- (3) a stable investment-grade credit rating; and
- (4) the Company's competitive position in the market place.

Accordingly, the Board will consider the medium-term business and credit rating outlook and provide for increased dividends if no suitable future growth opportunities or operational risks are identified.

It is noted that this policy needs to reflect the fact that, unlike a listed entity, Snowy Hydro cannot obtain new equity should an unexpected or unplanned opportunity arise, or in the

event that a deterioration in NEM or hydrological conditions is material enough to endanger Snowy Hydro's investment grade credit rating (an issue that a listed entity would be able to remedy with new equity).

It is also noted that, while the target dividend payout ratio is a five year average of 70 per cent or more of NPAT, the Board will consider variations based on specific proposals from Management. Preference will be given to retaining funds for investments where this can be argued to significantly enhance future shareholder value.

4.2 The Company's Credit Rating

In protecting Snowy Hydro's value, the single most important driver of dividend payments, development capital expenditure and debt levels is the need to protect the company's status as a creditworthy counterparty in the NEM. Snowy Hydro's contracting counterparties in the NEM demand an investment grade credit rating since the contracts that are best suited to Snowy Hydro's capabilities and are most financially attractive are long-term, credit-intensive contracts that expose the counterparties to Snowy Hydro's creditworthiness over an extended period. This is particularly relevant for capacity-type contracts under which up-front premiums are paid to Snowy Hydro.

The dividend policy acknowledges the over-riding requirement to maintain a strong investment-grade credit rating (taken to be BBB+ from Standard & Poors).

Maintaining a strong investment-grade credit rating remains of primary importance to underpin the Company's wholesale contracting activities. The Board will ensure that, in determining its annual dividend payment, the Company will maintain at least a strong BBB credit rating without the need for additional shareholder equity. Dividends will be calculated as a proportion of NPAT before adjustment for the mark-to-market of derivatives. The shareholders acknowledge that NPAT will include adjustment for the fair value of derivatives.

5. OBLIGATIONS AND RISKS

Many new obligations and risks have been created in the course of, and as a result of, corporatisation. Now largely concluded is the task to fully understand, quantify and respond to these different conditions. A substantial risk management and compliance infrastructure has been developed and is proven to meet these new conditions.

However, significant other risks continue to arise from:

- (1) the age of plant and equipment;
- (2) maintenance issues;
- (3) an environment of change impacting on corporate and supplier knowledge;
- (4) the state of communications and controls technology and facilities;
- (5) the difficult working environment of the Snowy Mountains;
- (6) the challenges of operating in a national park, particularly KNP; and
- (7) the physical separation of the Sydney trading activities from the dispersed

generation sites.

Foremost, however, with regard to severity and likelihood is arguably transmission risk.

Formal risk assessment processes are in place. Priority is given to responding to those risks arising from transmission, from the market, from environmental obligations and from occupational health and safety obligations.

Substantial regulatory risks exist across the business. While strategies exist to mitigate the impact of changes once they are known, there is sometimes little that can be done by way of adequate offset. Such examples might include the substantial negative financial impact of NEM rule changes and the inflexibilities imposed by any new water release constraints.

While maximising the commercial value of the business, the Company will consistently and reliably meet its water release obligations under the Snowy Water Licence and each Annual Water Operating Plan approved under it.

6. SHAREHOLDER REPORTING AND RELATIONS

The *Constitution* of Snowy Hydro provides that the business of the Company is to be managed by or under the direction of the Board. The Board may exercise all powers of Snowy Hydro, subject to the limitations prescribed by the *Corporations Act 2001 (Cth)* ("**Corporations Act**") and the *Constitution*.

The *Constitution* imposes formal shareholder reporting obligations on the Company that are in addition to those required under the Corporations Act. Those obligations are:

- (1) to provide shareholders with a Corporate Plan annually for comment, and to report half yearly on the financial and non-financial performance of the Company against its Corporate Plan (among other things); and
- (2) to ensure continuous disclosure of:
 - (a) any significant amendments to the Corporate Plan adopted by Board resolution;
 - (b) any matters that may significantly affect the achievement of objectives in the Corporate Plan; and
 - (c) any information concerning the Company that a reasonable person would expect to have a material effect on the price or value of shares in the Company.

The *Constitution* also requires that:

- (3) the Company obtain shareholder approval before undertaking a number of matters including changing the nature and scale of its activities, disposing or winding up of its main undertaking or appointing an external administrator; and
- (4) the Board consult with the shareholders prior to undertaking certain activities including, for example, acquiring any major debt, asset or investment (other than any acquisitions referred to in a Corporate Plan), lending funds to third parties or

approving the undertaking of any material capital or financial restructuring.

In addition, the Company initiates shareholder briefings from time to time to ensure not only that the Company's obligations to seek shareholder approval under the Corporations Act are fully satisfied, but that shareholders, each having equal voting rights, continue to have a sound understanding of the Company, its operations and its business development objectives.

Specifically, at briefings in February and August each year, the Company will report on performance, progress and outlook compared to the then current Corporate Plan. Such reporting will include comparison and comment in relation to EBIT, PBT and dividends/capital returns along with ratios of RoA, RoE and non-financial measures such as those relating to plant performance, environment and safety, and water release progress.

In addition, shareholder briefings will be provided in May and November with regard to performance, progress and outlook compared to the then budget and 12 month outlook.

7. CODE OF CONDUCT

The Company has formally adopted a Code of Conduct covering Directors and all employees.

The Company demands high standards of transparency in all its dealings. It also expects the "spirit" of the law to be followed, not just the "letter".

With regard to obligations relating to Occupational Health and Safety, ACCC, AER, EPA, Equal Employment Opportunities and Anti Discrimination legislation, the highest standards are expected.

8. BENCHMARKS

8.1 Financial Measures

The Company aims to be in the top quartile of the industry participants in the NEM with regard to shareholder value growth and return on assets employed. Due to the commercially sensitive nature of financial forecasts, they have not been included in this *Statement of Corporate Intent*.

8.2 Non- Financial Measures

The Company has a suite of non-financial measures by which to evaluate and determine its project and improvement initiatives and by which it is able to monitor its performance. Performance is assessed on an individual, team and corporate basis.

Snowy Hydro monitors eight key corporate non-financial performance measures as follows:

Measure	Limit
Hydro generation start reliability (%)	>99.4
Hydro generation forced outages during peak periods (%)	<0.55

Gas generation start reliability (%)	>95
Gas generation forced outages during peak periods (%)	<2.0
Snowy Scheme annual water release compliance (deviation from Required Annual release – gigalitres)	> -40
EPA notifiable events (number)	0
Lost time injuries - Snowy Hydro employees (number)	≤1
Lost time injuries - Red Energy employees (number)	≤1

The Company's water release obligations are set out in each Annual Water Operating Plan. The Company reports publicly each year on performance against these obligations.

9. ACCOUNTING POLICIES

Snowy Hydro's financial statements are prepared in accordance with International Financial Reporting Standards (A-IFRS), other authoritative pronouncements of the Australian Accounting Standards Board, Urgent Issues Group Consensus Views, and the Corporations Act.