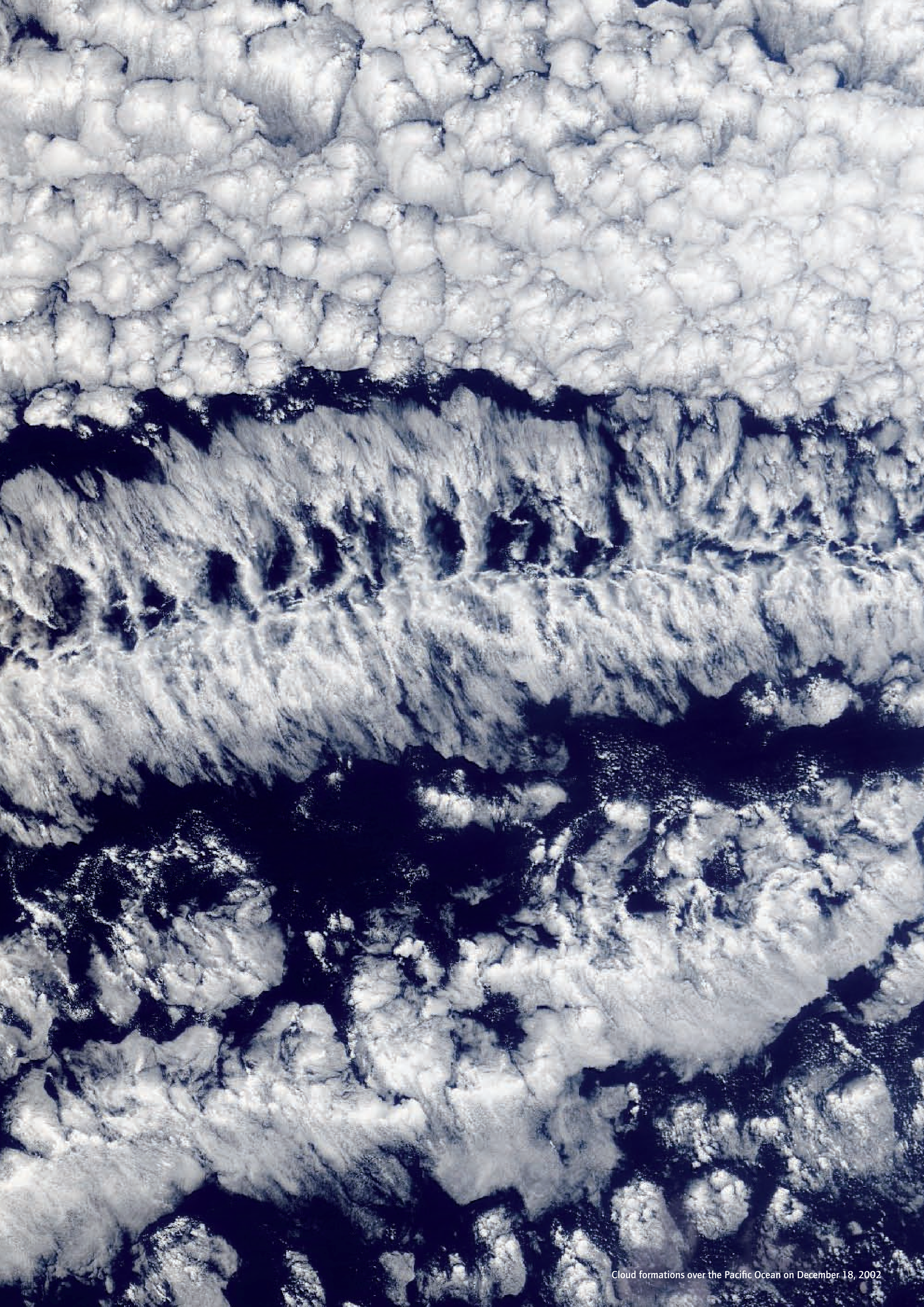
Meridian Energy Report for the six months ended December 2006



Cloud formations over the Pacific Ocean on December 18, 2002

Contents

Highlights

Customers

- Corporate customers have benefited from relatively low spot prices.
- New initiatives to promote energy efficiency in the home – a second light bulb offer to Christchurch customers and five $10,000 prizes for "home makeover" winners.
- Annual increases in electricity charges for residential and business customers held below the rate of increase in the consumer price index.
- Campaign to acquire South Island farm customers and to share the benefits of on-farm energy efficiency.
- Meridian Energy Irrigation Manager rolled out to more dairy producers.
- The launch of a major programme to roll out innovative new smart meter technology to 112,000 customers.
- Continued strong focus on high quality service through help desks, business/corporate account management and customer communications.
- Customer satisfaction indicators maintained at high levels.

People

- Continued strong focus on health, safety and wellness – no lost-time injuries among Meridian Energy staff in the half year.
- Maintenance engineers and technicians brought onto direct employment contracts – Meridian Energy's core capability strengthened with total full-time equivalent staff increasing to 428.
- Engineering graduate recruitment programme launched – increased support for electrical apprenticeships.
- Ongoing development of a competence framework for all staff, supported by thoroughly-planned induction and training programmes. New staff recruitment services now "in-sourced" by Meridian Energy.

Environment

- Open dialogue and consultation continued on the environmental and social impacts of major projects, most notably Project Hayes, the North Bank Tunnel Concept and the Hunter Downs Irrigation Scheme.
- Ongoing strict compliance in the operation of the Waitaki and Manapouri hydro stations and the Te Āpiti wind farm.
- Strong focus on energy efficiency initiatives that will help limit New Zealanders' energy consumption and carbon emissions.
- Participation in the international carbon credits market – credits allocated to the White Hill wind farm sold for use by Switzerland under the Kyoto Protocol on Greenhouse Gas Emissions.

Responsibilities

- Strong operating performance led to net profit after tax of $104.5 million for the half year.
- Solid progress made on major projects for new renewables generation that serve New Zealand's need for economically-efficient electricity supply at reduced levels of national carbon emission.
- Community funds allocated in the Te Āpiti and Waitaki areas – Meridian Energy continues to deliver on its commitment to local generation communities.
- Substantial dividends to the Government shareholder – a total of $1.1 billion paid during 2006.

Reputation

- Principal sponsorship of Project Crimson – Meridian Energy took on its first major environmental sponsorship.
- New Zealand Dairy Industry Awards added to the Company's broad portfolio of sponsorships.
- Meridian Energy's high standing in local and international financial markets recognised with an agreement on $700 million of more flexible, lower cost bank borrowing facilities.

Chairman and Chief Executive's Review

Meridian Energy continues to create and deliver the value of renewable energy for New Zealand. In the half year ended 31 December 2006, we:

- Achieved a net profit after tax of $104.5 million
- Held energy charge increases below the annual inflation rate
- Promoted energy efficiency in homes and businesses
- Developed renewable energy projects that help secure national electricity supply and deliver economic value over the long term
- Led this country's participation in international carbon markets – agreement on $9 million sale of carbon credits
- Paid a further $300 million dividend to the people of New Zealand

	Half year ended 31 Dec 2006	Half year ended 31 Dec 2005
New Zealand net energy revenue [1]	$345.0 m	$318.0 m
Net profit after tax	$104.5 m	$752.9 m [2]
Normalised net profit after tax	$104.5 m	$113.8 m [3]
Normalised EBITDA [4]	$247.1 m	$236.9 m

1. Excludes transmission and distribution charge recoveries.
2. Includes Southern Hydro operating results and all sale related gains/costs.
3. Excludes Southern Hydro operating results and gain on sale, sale costs, reduced interest costs, interest income and foreign exchange gains that resulted from the Southern Hydro sale.
4. Earnings before interest, tax, depreciation and amortisation, normalised for the 2005 half year by excluding Southern Hydro operating results.

Performance

Financial Results

Meridian Energy made a net profit after tax of $104.5 million for the half year ended 31 December 2006, based on strong operating performance. The Company increased New Zealand net energy revenue to $345 million, up 8.5% from the previous corresponding half year. This reflected positive conditions for hydro generation between July and December 2006 and relatively low wholesale electricity prices (see 'Operating Conditions'). Meridian Energy's generation for the period was 6050 GWh, up 1.5% from the 2005 half year.

Financial results for the previous period included the sale of Southern Hydro in November 2005. When the operating results of Southern Hydro and the non-recurring benefits of the sale are excluded, Meridian Energy made a normalised net profit after tax of $113.8 million for the half year ended 31 December 2005. The latest half year result was down to $104.5 million due mainly to a significant increase in depreciation expense ($15 million) after revaluation of the Company's generation structures and plant assets as at 30 June 2006 (the outcome of this revaluation increased the carrying value of these assets by $1.8 billion).

Meridian Energy's strong operating performance for the 2006 half year was reflected in EBITDA[4] of $247.1 million, which increased 4.3% from the 2005 half year (on a normalised basis).

Operating Conditions

National hydro generation inflow and storage levels improved substantially during the half year, after an extended period of low inflows through the summer and autumn of 2005-06 raised the spectre of a power supply shortage last winter. Higher inflows from May 2006 onwards eased the supply position and by November, national storage was 130% above the seasonal average level. Spring snow melt and rainfall accelerated recovery in the Waitaki lakes and the half year ended with their storage at 117% of seasonal average and 69% above December 2005. Meridian Energy's share of national generation during the half year was approximately 30%.

Electricity demand continued to grow. Average weekly demand through July-December 2006 was 1.9% higher than in the previous corresponding period (PCP). However, wholesale market prices were lower against PCP due to the recovery in hydro inflows and storage and the avoidance of any significant thermal plant or transmission system outages. On average, spot prices were 40% down in the latest half year with the average across key reference points for the month of December 2006 down to 1.94c per KWh (compared with 11.6c in December 2005).

Plant performance

The operational performance of Meridian Energy's hydro stations continues to be very high. During the half year plant availability was higher than target level, reflecting the effectiveness of maintenance activity. There were also no major forced outages.

	Half year ended 31 Dec 2006	Half year ended 31 Dec 2005
NZ generation volume	6,048 GWh	5,960 GWh

The Te Āpiti wind farm continued to operate below the availability target, established by turbine manufacturer Vestas due to mechanical problems with a small number of turbines. These problems are being rectified by Vestas, under the terms of its five year warranty agreement with Meridian Energy. Technical teething problems of this kind are not uncommon in the first years of operation of any major new generation plant.

Market Initiatives

Meridian Energy implemented an average 3.25% increase in energy charges (across all residential and small/medium enterprise customers) during the half year. Ministry of Economic Development analysis in November 2006 showed that Meridian Energy's charges in the residential and business markets were the lowest among all energy retailers in 22 of the 44 network pricing regions throughout New Zealand.

Meridian Energy offers corporate customers the option of taking direct exposure to spot prices in the wholesale electricity market. These customers benefited during the half year from periods of relatively low spot prices.

Meridian Energy is putting an increased emphasis on the rural sector, in recognition of the importance of energy supply to dairy production and other farm enterprises. During the half year, the Company launched a campaign to acquire additional customers among South Island east coast farmers who use irrigation. Meridian Energy account managers called at many properties to discuss energy usage and cost, along with the potential for on-farm energy efficiency gains and for greater certainty under fixed price contracts. The Company succeeded in acquiring new customers who together represent more than 100 GWh in the volume of electricity supply into this target market. The Company will continue to develop such customer relationships and promote Meridian Energy's role as a provider of energy solutions to farm enterprises. These solutions are through improved account management training and new product delivery.

Energy efficiency remains a key focus in residential markets. During the half year, the Company continued to promote energy efficient light bulbs for use in household lighting. Approximately 80,000 of these bulbs were sold as Christchurch residents took up a special pricing offer similar to the initial, extensive campaign in 2005. In the latest period, Meridian Energy also ran a "home makeover" competition promoting the value of energy efficiency in the household sector. Five customers who entered the most effective proposals for improving efficiency in their own homes received $10,000 each to implement their proposals. The competition attracted a high response in all areas where Meridian Energy supplies residential customers.

During the half year, customer surveys indicated a generally high level of satisfaction with Meridian Energy (see below). This reflects the Company's commitment to maintaining high quality help desk services, corporate and business account management services, and customer communications.

CUSTOMER SATISFACTION

	Residential and small business	Business	Corporate
Half years	Percentage of "good, very good and excellent" responses		
Dec 06	86	81	88
June 06	86	84	82
Dec 05	88	81	80
June 05	86	77	83

Energy Efficiency

Energy Solutions

Meridian Energy is developing a new business which will provide solutions for greater energy efficiency in the built environment throughout New Zealand. The new business will offer architects, builders and house buyers technical knowledge and products for new building projects to make them more energy efficient. Initial investment in improving the "energy performance" of a house can bring substantial benefits over time, in more comfortable and healthier living environments and in reduced energy consumption costs. The business will be launched later in 2007, with the initial focus on solutions for new houses. In future, we expect to extend the solutions approach to energy efficiency and heating to the design and construction of commercial buildings and to the renovation of older homes.

Smart Metering

During the half year subsidiary company Arc Innovations began deploying smart meters among residential and business customers in the Orion network in Christchurch and South Canterbury. Meridian Energy will replace existing meters with smart meters in 112,000 households in these areas over a two-year period. In time, the technology is expected to revolutionise energy usage in many homes and businesses. It should also provide a platform to transform the service electricity retailers can provide to residential market customers.

Dairy Sector Initiatives

Meridian Energy continues to build its focus on energy efficiency in dairy production. Meridian Energy Irrigation Manager offers farmers much greater control of both electricity and water usage in their irrigation systems. The Company will continue to demonstrate its potential to farmers who have their electricity supply on time-of-use metering in Canterbury and other regions. In 2007, we plan to once again have a strong presence at agricultural fieldays to promote on-farm energy efficiency. Consistent with this, Meridian Energy has become a National Sponsor of the New Zealand Dairy Industry Awards.

Community Programmes

Project Crimson

Meridian Energy became the principal sponsor of Project Crimson, an organisation established to conserve and protect two of New Zealand's iconic tree species, the pohutukawa and the rata. The Project Crimson Trust supports replenishment of the red-blooming natives in indigenous areas of the country where they have high environmental and cultural value and it promotes awareness of tree conservation in general. This is Meridian Energy's first major environmental sponsorship – one that is particularly fitting given the prominence of rata flowers in the Company's advertising on the theme of renewable energy.

Community Funds

Meridian Energy is delivering on its commitments to local communities near its generation assets. During the half year, the first funding allocations were made from the Waitaki Community Fund, established by the Company in partnership with local people in the Waitaki region. The Waitaki Fund allocated $83,000 to nine community projects, including projects at the Lake Tekapo and Twizel Area Schools, the Omarama Volunteer Fire Brigade and the Waitaki Valley Medical Trust. The Company has also established Community Funds for the communities near the Manapouri power station and the Te Āpiti wind farm.

Major Projects

West Wind

Meridian Energy awaits an Environment Court decision on an appeal against consent for Project West Wind – the 210MW wind farm planned to the west of Wellington City. Consent was granted in December 2005 with a substantial body of public submissions in favour of the project. Subject to the Court's decision, Meridian Energy is ready to proceed on this project expeditiously. Boasting one the world's best wind resources, the West Wind site is ideal for the generation of power from wind.

White Hill

Construction of the White Hill wind farm in Southland remains on track, with the site expected to produce first power in May 2007. During the half year, foundations were completed for all 29 turbines and 10 towers were erected. Site works continued through the winter with only four days lost due to poor weather. The 58MW wind farm will supply power to distribution networks in Southland.

In late 2004, Meridian Energy succeeded in submitting Project White Hill to the Government's Projects to Reduce Emissions tender round by demonstrating that the Project offered emission reductions additional to business as usual. This enabled the Government to allocate Kyoto credits to the project. The projected revenue from the sale of those credits was a key factor in Meridian Energy's commitment to build the wind farm. During the half year, we concluded negotiations on a sale of these credits worth more than $9 million over six years. The buyer is the Swiss-based Climate Cent Foundation, which has a procurement agreement with the Swiss Government to assist in meeting Switzerland's compliance obligations under the Kyoto Protocol on Greenhouse Gas Emission.

Project Hayes

Hearings on resource consent for the proposed Project Hayes wind farm are expected to be held soon. Meridian Energy applied for consent in mid 2006 and has continued to consult with all interested parties. The project involves a 630MW wind farm to be built in stages on the Lammermoor Range, Northern Central Otago. The Company has substantial indications of support from local groups although the proposal has also attracted some vocal opposition in the wider Otago area.

Waitaki Schemes

Meridian Energy has applied for new water use rights on the Waitaki in respect of the North Bank Tunnel Concept and the Hunter Downs Irrigation Project. Meridian Energy seeks to secure access to water as a prudent step before more extensive detailed design investigation and planning work is commenced. The North Bank Tunnel, taking water from behind the existing Waitaki Dam and passing it through an underground station, would add as much as 260MW of generating capacity to the Waitaki chain with limited disruption to the natural environment. The Hunter Downs Irrigation project would irrigate 40,000 ha of farmland between the river and Timaru.

North Otago Irrigation

The Downlands irrigation project was completed with Meridian Energy being the catalyst for the project by underwriting 1,500 hectares of the 1,000 hectare scheme. This brings water to the very fertile soils around Oamaru, a conclusion that has been sought for by farmers for 100 years.

Plant Refurbishment

Good progress continues to be made on the mid-life refurbishment of the Manapouri station, with the project now more than 95% complete. Final completion is due in October 2007, within the project budget of $98.1 million. Refurbishment of the Benmore station is proceeding through its early stages, with some contracts having been let in relation to the installation of new runners. A further significant project to enhance the seismic performance of the Aviemore dam was completed during the half year.

Comalco Negotiations

Negotiations continue on contracts for supply to Comalco's Tiwai Point aluminium smelter beyond 2012. During the half year steady progress was made in these negotiations and there is optimism on both sides that the basis for an agreement has now been put in place.

People

During the half year, the Company became the direct employer of maintenance staff based in Twizel and Manapouri. The 42 electrical engineers and technicians were previously employed at these sites by Transfield – a Meridian Energy contractor. Bringing this maintenance force inside the Company strengthens capability in a critical area of operations and facilitates the Company's commitment to the training and retention of people with specialist skills. With these employees included, Meridian Energy had 428 full-time equivalent staff at 31 December 2006 (up from 365 in June 2005).

The Company began an engineering graduate recruitment programme during the half year while also increasing its commitment to electrical apprenticeships. Further development work was done on a competency framework encompassing all staff and induction and training remained areas of high priority across Meridian Energy and its subsidiaries. There were no lost-time injuries among staff during the period, although four such injuries (including one serious) were reported among employees of contractors while on Meridian Energy sites. The Company seeks continuous improvement in health, safety and wellness policies and practices for all staff and for others who work on our sites.

Financial Position

Dividends

The Company paid a final $300 million dividend in October 2006. This brought the total amount distributed by the Company during 2006 to $1.1 billion.

Balance Sheet

Meridian Energy had total assets of $5.1 billion at 31 December 2006, including consolidation for the first time of the WhisperGen group of companies which became controlled entities in July. WhisperGen are developing and marketing micro-combined heat and power systems for domestic and commercial use.

During the half year, Meridian Energy successfully refinanced and restructured its bank borrowing facilities to enhance financial flexibility in this area and reduce funding costs. After a competitive tender process involving a range of banks, the Company has established $0.7 billion of new bank debt facilities. The positive outcome reflected Meridian Energy's high standing amongst domestic and international banks. The new facilities complement the Company's existing financing facilities and establish a solid financial platform for the Company's capital expenditure and investment programmes going forward.

Energy Strategy

Meridian Energy is committed to the vision of New Zealand as an international leader in renewable energy and in the use of advanced technologies for energy efficiency and reduction in carbon emissions. The Company's business direction reflects that vision, which is clearly evident also in the New Zealand Energy Strategy (NZES) announced in December 2006. The proposed NZES is a substantial step forward as this country – like many others – prepares for a future in which energy security and emissions reduction are key imperatives for governments, industries and citizens.

The NZES comes at a time of increasing concern in New Zealand and internationally about climate change. New Zealand is well placed to move forward to develop and adopt technologies to mitigate the threat and bring new competitive advantage to New Zealand within the global economy.

Outlook

The electricity supply outlook for the autumn and winter of 2007 is relatively good due to current hydro conditions and the planned commissioning of new generation plant. However the national demand continues to rise and generation reserves are still low by historical standards. The development of Meridian Energy's renewable projects are fundamentally important to New Zealand's energy security, climate policy and sustainable development objectives.

The Board acknowledges a very high level of commitment and skill among our staff. There are substantial challenges ahead but we are confident the Company has the strategy, assets and people to meet these.

Wayne Boyd
Chairman

Keith Turner
Chief Executive

Financial Statements

Statement of Financial Performance for the six months ended 31 December 2006

	NOTE	GROUP UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	 UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	 AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Operating Revenue	3	**887,825**	1,107,735	2,222,795
Operating Expenses		**(691,863)**	(887,127)	(1,819,881)
Financing Costs	4	**(27,921)**	(42,310)	(69,424)
Equity Accounting of Associate		**–**	–	(1,430)
Operating Surplus before Non-Recurring Items		**168,041**	178,298	332,060
Gain on Disposal of Subsidiary		**–**	652,516	652,516
Costs Relating to Disposal of Subsidiary		**–**	(25,575)	(26,879)
Net Surplus before Tax after Non-Recurring Items		**168,041**	805,239	957,697
Income Tax		**(63,591)**	(52,347)	(100,861)
Net Surplus after Tax		**104,450**	752,892	856,836
Net Surplus after Tax attributable to:				
Shareholders of the Company		**103,996**	752,892	856,836
Minority Interest		**454**	–	–
Net Surplus after Tax		**104,450**	752,892	856,836

Statement of Movements in Equity for the six months ended 31 December 2006

	NOTE	GROUP UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	 UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	 AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Equity at Beginning of Period		**4,237,351**	2,469,080	2,469,080
Post-Acquisition Assessed Retained Earnings of Controlled Entities	5	**542**	–	–
Restated Equity at Beginning of Period		**4,237,893**	2,469,080	2,469,080
Net Surplus after Tax attributable to:				
– Shareholders of the Company		**103,996**	752,892	856,836
– Minority Interest		**454**	–	–
Movement in Revaluation Reserve	5	**7,005**	–	1,800,000
Movement in Foreign Currency Translation Reserve		**(2)**	(9,164)	(9,159)
Total Recognised Gains and Losses		**111,453**	743,728	2,647,677
Dividends to Shareholders		**(300,000)**	(79,406)	(879,406)
Equity at End of Period		**4,049,346**	3,133,402	4,237,351

The Statement of Accounting Policies and Notes to the Financial Statements form an integral part of these Financial Statements.

Statement of Financial Position as at 31 December 2006

	GROUP		
	UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Equity			
Shareholders of the Company	**4,038,068**	3,133,402	4,237,351
Minority Interest	**11,278**	–	–
Total Equity	**4,049,346**	3,133,402	4,237,351
Liabilities			
Non-Current Liabilities			
Term Borrowings	**754,649**	754,649	754,649
Deferred Tax	**159,802**	155,311	152,089
Total Non-Current Liabilities	**914,451**	909,960	906,738
Current Liabilities			
Payables and Accruals	**123,955**	273,216	193,137
Current Tax Payable	**21,494**	24,849	2,085
Total Current Liabilities	**145,449**	298,065	195,222
Total Liabilities	**1,059,900**	1,208,025	1,101,960
Total Equity and Liabilities	**5,109,246**	4,341,427	5,339,311
Assets			
Non-Current Assets			
Investments	**14,612**	30,496	23,395
Prepayments	**8,322**	12,215	8,288
Intangible Assets	**24,693**	210	172
Customer Acquisition Costs	**19,458**	26,387	22,808
Property, Plant and Equipment	**4,830,741**	2,986,357	4,795,590
Total Non-Current Assets	**4,897,826**	3,055,665	4,850,253
Current Assets			
Cash and Bank Balances	**41,429**	1,025,055	251,824
Accounts Receivable & Prepayments	**160,404**	257,450	234,128
Inventories	**9,587**	3,257	3,106
Total Current Assets	**211,420**	1,285,762	489,058
Total Assets	**5,109,246**	4,341,427	5,339,311

The Statement of Accounting Policies and Notes to the Financial Statements form an integral part of these Financial Statements.

Statement of Cash Flows for the six months ended 31 December 2006

	NOTE	GROUP UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Operating Activities				
Cash was Provided from:				
Receipts from Customers		**952,162**	1,062,395	2,177,015
Net GST Receipts		**2,569**	4,886	1,145
Interest Received		**8,053**	7,308	39,488
		962,784	1,074,589	2,217,648
Cash was Applied to:				
Payments to Suppliers and Employees		**711,198**	790,692	1,755,320
Interest Paid		**27,885**	42,142	68,969
Income Tax Paid		**34,535**	28,700	103,170
		773,618	861,534	1,927,459
Net Cash Inflows from Operating Activities	6	**189,166**	213,055	290,189
Investing Activities				
Cash was Provided from:				
Sale of Property, Plant and Equipment		**1,368**	922	5,314
Sale of Investments		**203**	416	2,181
Net Cash Proceeds on Disposal of Subsidiary		**–**	1,492,766	1,492,766
		1,571	1,494,104	1,500,261
Cash was Applied to:				
Purchase of Property, Plant and Equipment		**86,841**	23,788	75,980
Net Cash Outflows on Acquisition of Controlled Entities	5	**13,138**	–	–
Capitalised Interest		**739**	953	2,003
Purchase of Investments		**267**	3,415	6,700
Purchase of Intangible Assets		**147**	–	–
		101,132	28,156	84,683
Net Cash (Outflows)/Inflows from Investing Activities		**(99,561)**	1,465,948	1,415,578
Financing Activities				
Cash was Applied to:				
Dividends Paid		**300,000**	79,406	879,406
Current Portion of Term Borrowings		**–**	370,141	–
Term Borrowings		**–**	245,228	615,364
		300,000	694,775	1,494,770
Net Cash Outflows from Financing Activities		**(300,000)**	(694,775)	(1,494,770)
Net (Decrease)/Increase in Cash Held		**(210,395)**	984,228	210,997
Cash at Beginning of Period		**251,824**	40,827	40,827
Cash at End of Period		**41,429**	1,025,055	251,824
Composition of Cash				
Cash and Bank Balances		**41,429**	1,025,055	251,824

The Statement of Accounting Policies and Notes to the Financial Statements form an integral part of these Financial Statements.

Notes to the Financial Statements for the six months ended 31 December 2006

1. Basis of Preparation

The interim financial statements presented are the unaudited consolidated financial statements of the Group comprising Meridian Energy Limited and its controlled entities, for the six months ended 31 December 2006.

The financial statements included in this half yearly report have been prepared in accordance with FRS 24, *Interim Financial Statements*, and should be read in conjunction with the financial statements and related notes included in the 2006 Meridian Energy Limited Annual Report.

2. Statement of Accounting Policies

The accounting policies used in the preparation of these Group financial statements are consistent with those used in the preparation of the Group financial statements for the year ended 30 June 2006 and for the six months comparative period ended 31 December 2005.

Where necessary to facilitate comparison, comparative figures have been adjusted to conform with changes in presentation in the current period.

3. Operating Revenue

	GROUP		
	UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Interest Revenue included in Operating Revenue	**8,053**	7,308	**39,488**

4. Financing Costs

	GROUP		
	UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Interest on Borrowings	**28,660**	43,263	71,427
Less Capitalised Interest	**739**	953	2,003
Total Financing Costs	**27,921**	42,310	69,424

5. Acquisition of Controlled Entities

At 30 June 2006 the Group held a 31.3% investment in Whisper Tech Limited which was equity accounted as an associate and a 40% investment in the Whisper Tech joint venture held at fair value.

On 3 July 2006 the Group purchased the remaining 60% of the joint venture from Orion NZ Limited and all but 5% of Orion NZ Limited's interest in Whisper Tech Limited (44%) for $13.362 million. This resulted in the Whisper Tech group of companies becoming controlled entities from this date and as a consequence consolidated as part of the Meridian Energy Limited Group financial statements.

Summary of the Effect of Acquisition of Controlled Entities

	GROUP UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000
Assets and Liabilities acquired at fair value:	
Cash and Bank Balances	224
Accounts Receivable and Prepayments	1,985
Property, Plant and Equipment	2,027
Intangible Assets	22,687
Inventories	6,101
Current Tax Receivable	1,934
Payables and Accruals	(7,404)
Net Assets Acquired	27,554
Acquisition of Control Adjustments	
Investment in Whisper Tech Joint Venture	(8,149)
Gain Recognised on Investment in Whisper Tech Joint Venture	(239)
Investment in Associate – Whisper Tech Ltd	(716)
Post-Acquisition Assessed Revaluation Reserve of Controlled Entities	(7,005)
Post-Acquisition Assessed Retained Earnings of Controlled Entities	(542)
Total Acquisition of Control Adjustments	(16,651)
Goodwill Arising on Acquisition	2,459
Total Cash Paid	13,362
Cash Included in Net Assets Acquired	(224)
Net Cash Paid on Acquisition	13,138

Notes to the Financial Statements for the six months ended 31 December 2006 (continued)

6. Net Cash Flow from Operating Activities

	NOTE	GROUP		
		UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Reconciliation with Net Surplus after Tax				
Net Surplus after Tax		**104,450**	752,892	856,836
Items Not Involving Operating Cash Flows				
Depreciation Expense		**53,577**	44,521	83,486
Amortisation		**4,872**	15,879	19,496
Surplus Attributable to Minority Interest		**(454)**	–	–
Deferred Tax		**7,713**	1,055	(2,167)
Net (Gain)/Loss on Sale of Property, Plant and Equipment		**(524)**	(503)	149
Gain Recognised on Investment in Whisper Tech Joint Venture	5	**(239)**	–	–
Gain on Sale of Investments		**(18)**	–	–
Write Down of Investments		**–**	–	7,191
Equity Accounting of Associate		**–**	–	1,430
Other Non-Cash Items		**(297)**	–	–
		64,630	60,952	109,585
Changes in Working Capital Items				
Accounts Receivable and Prepayments		**73,724**	30,300	57,549
Inventories		**(6,481)**	121	272
Payables and Accruals		**(69,182)**	(32,938)	(113,017)
Current Tax Payable		**19,409**	22,592	(172)
Net Working Capital of Controlled Entities Acquired		**2,616**	–	–
Net Working Capital of Subsidiary Disposed		**–**	31,652	31,652
		20,086	51,727	(23,716)
Items Classified as Investing Activities				
Gain on Disposal of Subsidiary		**–**	(652,516)	(652,516)
		–	(652,516)	(652,516)
Net Cash Flow from Operating Activities		**189,166**	213,055	290,189

7. Commitments

	GROUP		
	UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Capital Expenditure			
Commitments – Contracts for Capital Expenditure	**37,921**	4,804	74,414

8. Use of Financial Instruments

The policy guidelines set by the Board of Directors to manage derivative financial instruments have not changed during the six months to 31 December 2006.

Interest Rate and Currency Instruments

The principal or contract amounts outstanding at balance date are as follows:

	GROUP		
	UNAUDITED 6 MONTHS ENDED 31 DEC 2006 $'000	UNAUDITED 6 MONTHS ENDED 31 DEC 2005 $'000	AUDITED 12 MONTHS ENDED 30 JUNE 2006 $'000
Cross Currency Interest Rate Swaps	**704,649**	704,649	704,649
Forward Exchange Contracts	**53,775**	109,756	81,274
Interest Rate Swaps	**635,500**	700,500	735,500
Interest Rate Options	**–**	–	20,000
Interest Rate Collars	**65,500**	–	–
Foreign Exchange Options	**338,578**	–	–

Electricity Derivatives

As part of its energy portfolio contracts, and as part of its wholesale risk management activities, the Group has electricity derivatives with counterparties for various periods out to 2013. The face value of outstanding electricity derivatives in New Zealand at hedge prices is $156.1 million as at 31 December 2006 (31 December 2005 $207.6 million).

9. Contingent Gains and Losses

Other than contingent liabilities arising in the normal course of business, the contingent gains and losses of the Group arising in the financial period to 31 December 2006 are as follows:

- The Group has been the subject of an Inland Revenue audit and some positions have been disputed by Inland Revenue. However, the Board are of the opinion that the approach taken in calculating the Group's tax liability as reflected in these financial statements is acceptable. The Group is defending the adjustments that Inland Revenue has proposed.

10. Impact of adopting New Zealand Equivalents to International Financial Reporting Standards

The Group will adopt NZ IFRS for the year ending 30 June 2008. Transition from existing NZ GAAP to NZ IFRS will be made in accordance with NZ IFRS 1 *First-time Adoption of New Zealand Equivalents to International Financial Reporting Standards.* Upon adoption of NZ IFRS, comparative information will be restated to conform to the requirements of NZ IFRS and the impact that adoption of NZ IFRS has had on the Group's financial statements will be disclosed.

The Group is well advanced in evaluating the impact of NZ IFRS on its financial statements. The key areas identified that have a significant impact on the opening NZ IFRS comparative position of the Group are outlined below.

The impact of adopting NZ IFRS will only be finalised when the first complete set of NZ IFRS financial statements are prepared as at 30 June 2008. Until this time the NZ IFRS standards and the application of those standards may be subject to change.

While every effort has been made to quantify and disclose the potential impacts of adopting NZ IFRS, the actual impact of adopting NZ IFRS may vary from the information presented below and the variation may be material.

Financial Instruments

NZ IAS 39: *Financial Instruments Recognition and Measurement* governs the recognition requirements for financial instruments. The Group enters into derivatives primarily to manage exposures to interest rate, foreign exchange and electricity price risk. On transition to NZ IFRS the Group is required to record derivatives on the balance sheet at their fair value. Subsequently these derivatives are accounted for at fair value at each accounting period, with changes in fair value reflected in the income statement or, in respect of cash flow hedges, in equity if NZ IAS 39 hedge accounting criteria can be met. To the extent that hedge accounting does not apply, there is potential for profit volatility resulting from the application of NZ IFRS.

The Group has designated certain derivatives as either:

Fair Value Hedges – hedges of the fair value of recognised assets or liabilities or commitment; or

Cash Flow Hedges – hedges of highly probable transactions.

Electricity Derivatives

The Group is a party to a number of electricity derivative contracts and where material has designated these derivatives as cash flow hedges. On transition to NZ IFRS the Group will recognise the fair value of the derivatives on the balance sheet with subsequent changes in fair values reported in equity, or in the income statement if hedge accounting criteria are not met. The expected impact on transition to NZ IFRS at 1 July 2006 is an increase to equity and net assets of approximately $8.4 million, prior to adjusting for deferred tax.

Treasury Derivatives

The Group has a number of treasury derivative financial instruments in place. On transition to NZ IFRS the Group will recognise the fair value of these derivatives on the balance sheet. Where appropriate the Group will seek a hedge accounting outcome designating these derivatives as either fair value or cash flow hedges. To the extent that hedge accounting is not possible or is not applied there is potential for profit volatility resulting from the application of NZ IFRS. The group is currently in the process of determining the financial impact of applying NZ IAS 39 in relation to these treasury derivatives.

Deferred Tax

NZ IAS 12: *Income Taxes* requires a "balance sheet" approach to deferred tax, recognising all differences between tax and accounting values, with limited exceptions. This is conceptually different to the current NZ GAAP "income statement" approach. Many items, previously considered permanent differences under NZ GAAP, now become temporary differences and result in the recognition of a deferred tax liability.

The most significant impact of the application of this standard is the recognition of a deferred tax liability in relation to the asset revaluation reserve on transition to NZ IFRS at 1 July 2006, which is expected to result in the recording of a deferred tax liability and a corresponding reduction in equity of $824 million.

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