Meridian Energy Investor Briefing 18 Jan 2021

OWEN HACKSTON ===Good morning. It is Owen Hackston speaking, Meridian's Investor Manager. Welcome to todays call, which follows on from last week's announcement of a contract extension agreement between Meridian and NZAS. I'm here in Wellington with Neal Barclay, Meridian's Chief executive. Mike Roan Meridian CFO is on the line, rather symbolically calling in from the Manapōuri power station. You may be reassured our CFO spends holidays inspecting the company's generation assets. It is also Mike's birthday today. I'm sure he could think of no better way of celebrating than doing an investor call. For the call, Neal and Mike will talk through the business update that accompanied our market announcement last Thursday, and then we will take questions. When Neal indicates we are ready for questions, the operator will come onto the call and outline the process for asking questions. Neal, over to you.

NEAL BARCLAY>> Thanks, Owen and welcome, everyone on the call. The purpose of this call is to provide some insight into the amended four-year deal that we have concluded with NZAS and announced to the market last week on Thursday. We have worked hard to provide solutions that we believe are of lasting value to the smelter and acceptable to our shareholders. We are delighted that Rio Tinto has accepted the terms of this extended closure offer, which provides certainty for the Southland community and the time that the industry needs to do the best job to transition to the new future. I will start with recapping background on how we got to this point.

On 9 July last year, NZAS gave Meridian that they would cancel the existing electricity agreement effective at the end of August 2021. In doing so, they chose to decline a number of contractual amendments that Meridian already offered, that we believed would have offered significant value to the smelter and ensure it would remain a viable operation for many years to come. We talked about those amendments on our investor call last July. Having received the cancellation notice, on 17 July, Meridian put a firm offer to NZAS that gave them an option to extend the closure date of the smelter to end of August 2024. The pricing of that offer was of a significant discount to any price conversations we'd had with NZAS up to that point and reflected the fact that if the closed in August 2021, then transmission constraints and transmission losses would lead to higher levels of spill and lower generation revenues from Meridian for a few years.

To ensure we created ourselves enough time to mitigate these impacts a cents and a dollar type arrangement made sense for Meridian. For that reason, the price included in the extended closure offer does not are a sustainable price for the electricity sector in New Zealand. This is an exit agreement and there is no option for NZAS to extend the contract beyond 2024.

While the price in that July 2020 offer did not change during subsequent negotiations, the terms of our extended closure offers were refined during December to allow NZAS to reduce the contract volume from 400 megawatts from 1 July 2022 and given the passage of time, to extended the term of the agreement to 31 December 2024. Now a 400 megawatt smelter works for us. In some ways it may be preferable towards the end of the four-years as we work with the Southland community to encourage new business into the region over that time.

We have not been part of the negotiations between the New Zealand Government and Rio Tinto regarding site and remediation and transmission costs but last Wednesday evening we received notice from NZAS and its owner that they would accept our offer and we were able to close on an amended contractual agreement that night. I will now hand over to Mike who will talk through the amended contract aspects in more detail.

MIKE ROAN>> Thanks, Neal. Just picking up on Owen's comments at the start there, it is a real privilege. This power station, this asset is a tremendous part of our business and it is quite nice to be having this conversation with investors on my birthday, certainly compared to the alternate. So I will talk to slide 2 of the presentation primarily. As I do, first it is important to remember that the agreement that we have with NZAS is contract difference and that agreement has been in place since 2013, being amended a couple of times since then, but the key point is it is a financial contract that provides price certainty for NZAS. It doesn't provide supply certainty and doesn't direct electricity from the power station to NZAS. Rather NZAS purchases electricity it requires directly from the wholesale electricity market alongside many other participants. By way of example of that is that in December 2020 Manapōuri generation was generally below consumption. This is similar to many other contracts in place with customers around New Zealand.

A second thing is a full copy of the contract can be found on Meridian's websites. The amendments are summarised in the presentation I will talk to in a minute, and will also be posted on the website so anyone can work their way through the detail by heading over there when they have time.

What we've agreed to do with NZAS is we’ve adjusted the underlying agreement as follows - We've adjusted the price and that price is fixed through the four-year term. To enable it we've removed the language in the agreement referred to in CPI escalation and aluminium price participation. We also introduced an option for NZAS to reduce consumption from 572 megawatts to 400 megawatts by providing us with six months' notice.

The first time they can do that is 1 January 2022, but based on our modelling and given current aluminium price and exchange rates, this deal will mean NZAS is likely to be profitable for 4 years. So the option really gives them some downside protection should aluminium prices trend down again and if they choose that option, also provides us with arguably a better transition as Neal mentioned.

The last thing that we changed of note in the agreement were the end provisions or force majeure provisions. These are a little complex, so I won't do justice to them here, but to summarise the changes, they previously required that for an order for NZAS to secure relief against contract quantity following an event of force majeure, that NZAS' response to the event has to be consistent with the nature and scale of response expected of a smelter with at least 10 years of operational life left, and that was reflected in the contract terms.

That meant that there is an exceptionally high bar for them to meet in terms of new investment, including any capital that they would have to potentially be required to make, and in our view, that wasn't any longer appropriate for a smelter that will close on 31 December 2024. So we have made changes to reflect and provide for response FM that is appropriate for a smelter with that remaining life through December, or up to December 2024. NZAS of course needs to do everything they can reasonably and safely be expected to do to restore consumption if they want relief against contract quantity.

If an event of force majeure (and this is already in the contract) reduces the smelter's ability to produce 400 megawatts, either NZAS or Meridian can terminate the contract on three months' notice. Other than that, all the other provisions like smelter demand response or key provisions like smelter demand response and price separation remain. We have also adjusted the terms of the backing contract that we have in place with Contact Energy. The 10-year agreement replicates the new term with NZAS. The price is different to the earlier contract, as is the volume which is now about 100 megawatts on average, unless NZAS elects to move to a 400mw smelter and that arrangement is pro rated with that agreement. I must say that without Contact’s support and commitment, we wouldn't have been able to form a new agreement with NZAS so I want to take a second on this call to say thanks to them as well.

Before handing back to Neal, I also want to cover the mitigations that we presented back when we talked to this topic in July and you will find them in the presentation back then where we covered three areas: Transmission, physical flexibility and there was portfolio flexibility.

First up, and this relates to transmission, as you will see on page 4 of this presentation, Transpower is on track with taking up the Clutha-Upper Waitaki lines project and expect to complete it by May 2022, and like Contact, we would like to note they were incredibly proactive back in 2020. TransPower, that is, and mobilised very quickly to focus on this upgrade and showed what can be done when things change.

Back in July, we also noted weren't overly concerned about sending energy across the HVDC link, our focus was primary between Southland and Canterbury, but that there were limitations in the North island reserves market that required some attention should NZAS exit. So at that time we tabled a proposal to build a 100 megawatt battery that could and would provide those reserves. I think at the time I said the economics were a no machine brainer for that battery should NZAS exit, and the good news is they continue to look positive. But, of course, if we succeed in finding a home for all of the NZAS consumption through new sources, then the economics don't look as compelling, so we are thinking about it in terms of an insurance option that we will commission prior to NZAS closure, depending on where we are with that new demand.

The closure delay is, of course, beneficial in two ways actually in that the first we expect that there would be new generation of battery technology to emerge in the next couple of years which should be useful from that perspective and we are confident that 100 megawatt-hour battery can be deployed with in the 2024 timeframe. When it came to physical flexibility, what we talked about was lake Pukaki storage and how we've been able to add a further 367 gigawatt hours to that storage. That was done in November 2019, so I won't talk to that any more here, really just repeating that message, and portfolio flexibility was threefold.

We talked about swaption with Genesis which terminates end of December 2022. With the news last week, we will recommence deliberations for a replacement of that swaption, noting that Harapaki provides us flexibility should we choose to build that wind farm and/or we struggle to engage with counterparties for any new type swaption. Wholesale sales, we noted back in July we made about 50 megawatt ASX sales from September 2021 through to 2023. They obviously aren't as important as we thought back then.

The last thing we talked to was how we continue to grow our retail business. Our operating stats will be out next week for the first six months of this financial year and Neal and I will talk to this more generally when we present our interim statements, but it's fair to say that we continue to grow our retail business and four years provides us with ample time to build and manage our portfolio, subject to new supply in Southland. That's pretty much it from me. Neal, I will hand it back to you.

NEAL BARCLAY>> Cheers, Mike. We are very comfortable with the way our mitigation strategies to encourage new demand in the region are progressing. I will just touch on each of the main, if you like, the big-ticket potential items and how we are going with them.

Process Heat - we've completed high-level assessments looking at converting fossil fuel heat process to electricity. This includes looking at small and large-scale opportunities across a number of different industries. We've also worked with counterparties to understand the transmission requirements needed to get these projects off the ground. I think these opportunities represent a renewed interest by these sectors in decarbonisation of process heat and it is looking encouraging.

I think long-term contracts with sustainable NZAS type pricing will get many of the smaller scale decarbonisation projects over the line and we think the opportunity could be at much as 250 to 500 gigawatt hours just in that sector, so you can expect to hear much more about that as we progress.

IT Infrastructure: We have been working alongside the data grid team since August last year on what will eventually be potentially a 100 megawatt data centre in Southland connected by fibre-optic cable with the east coast of Australia. The proposition looks positive and it is progressing ahead of plan. We understand that Remi Galasso and his team have land options secured and have started engineering work on the facility. The significant next step will be securing the first customer.

Green hydrogen: I realise there are many sceptics around the economic viability of green hydrogen, but the interests we are seeing from a large number of credible players suggest that the opportunity for the export and production of green hydrogen is realistic. The race to secure what will become a massive market is on. We are developing a process to consider the current multiple proponents who we are engaged with and to attract other possible partners as well.

And in parallel with that process, Meridian and Contact have initiated a $2 million dollar joint study into green hydrogen. There are three key aspects to that study: One, the market analysis and economics. Two, site engineering costs and scale, plant flexibility, product storage and transport, and Three, flexibility benefits to the power system, ie dry-year storage and a contribution to the New Zealand battery initiative.

Whatever we come up with, the economics of a scale hydrogen production facility in Southland starts to look like a no-brainer, if the facility can also provide demand response services to the electricity industry. Seasonal response is likely to not only a viable option for the provider, but also a very efficient option for the New Zealand electricity system to manage system security as our reliance on gas and coal diminishes. Mike has already referred to the Clutha Upper Waitaki lines project so I will move onto the summary page here.

To sum up, we are obviously very happy to conclude arrangements to extend the closure of the smelter out to December 2024. It was clearly in our commercial interests to do so, but it was also a very good outcome for the Southland region of NZ and it will provide all concerned, certainty and time to manage the transition. I think the transition itself will create many opportunities that will ultimately deliver greater benefits to New Zealand than exporting electricity in the form of aluminium. I'm personally very energised to start 2021 on these terms.

We will now take some time to execute on some really exciting opportunities for life beyond the smelter that will deliver new clean energy solutions that will benefit not only Meridian’s business but its customers and the wider economy.

The four-year deal also provides ample time for Transpower to continue their excellent progress delivering the necessary transmission enhancements, which along with the North Island reserve enhancement opportunities, ie the battery, will allow the NZAS to be exported from the lower South Island to the rest of New Zealand if those new demands are slow in arriving.

I guess the thing you're all wanting to know is what does this mean for Meridian's dividend. All I can tell you at this stage is that Meridian's dividend policy has not changed but noting that the existing policy does provide the board with a reasonable degree of flexibility. We will be in a better position to provide better guidance in our half-year results on 24 February and particularly you can expect to hear from us on the interim dividend for FY21, how we are thinking about flexibility of our balance sheet and the timing of our Harapaki wind farm option.

Just one final closing comment from me: Prior to last year, I personally would not have chosen for NZAS to exit New Zealand in 2021 or 2024, for that matter. Since they have taken that decision, it has driven us to seek out a raft of opportunities and if we can execute well, they will create a far more robust and diversified business. So whilst getting off the NZAS drug cold turkey would have been pretty tough. We do need to go drug-free. This four year transition period, given our inherent balance sheet strength, I believe it is very manageable and in the best long-term interests of our company. Now we can stop talking for a bit and take some questions.

ANNOUNCER>> To ask a question. Please press 01 on your key pad and wait for your name to be announced. There will be a short silence while we wait to you to be connected.

ANNOUNCER>> First question comes from Grant Swanepole. The line is open.

GRANT>> Good morning, team. Eventually we get a deal done. That's fantastic. First question is around your (INAUDIBLE) process you're talking about 250 to 500gwh it looks like fairly near term that opportunity could come up. With all the forward work you've put in place, how does the supply/demand balance looking without the Hakapaki build over the next few years.

NEAL >> Grant, a couple of aspects, that 250-500 gigs, it is reasonably near-term, but will take two to three four years to execute on, so it will take time. In terms of portfolio mix and position I will hand over to Mike to provide a bit more context to that.

MIKE>> Yes, really good shape, Grant. With the contract we've got in place and as those contracts they just give us analysis, so if we find high-value opportunities in the CNI space we might continue to roll them over, but if the new growth opportunities don't emerge then we will continue to do so but if the opportunity to grow new load, high value, then rolling over in the CNI biz then we will do that as well. So no concerns with the existing portfolio and the choices that we've got in front of us, with or without Harapaki is probably the key point.

GRANT>> Will we expect to see you guys ease back on the retail land grab over the last couple of years?

MIKE>> I think it has just been organic, Grant. It has come to the right value. It creates the margin for us above wholesale price rather than selling residual volumes into the spot market, we've chosen to sell to retail customers and just grow value organically that way. No, I think we're quite comfortable with the growth that we've seen in the underlying books. As I say, if we did see any particular challenge in front of us, we do have contracts rolling off all the time that just allow us (INAUDIBLE). We are very comfortable with the way we're tracking.

GRANT>> And my second question...

NEAL>> I was going to add, Grant, that growth in retail has been done at a profitable level, so it's sort of no regrets in some regards, and I don't see that easing up while we're successfully executing on it.

GRANT>> Thanks. I think the back-to-back contract with Contact is expected out later on this week. Should we consider the price, as you've said, with Contact is similar to the price you have with Rio, or does the flexibility in the Contact contract mix it up a little bit.

MIKE>> Grant, I think it would be wrong for us to comment on contract price that we've got with Contact with how that compares to the contract price that we put in place with NZAS

GRANT>> Thanks, Mike. Thanks, Neal.

NEAL>> Cheers, Grant.

>> Our next question comes from Andrew Harvey-Green. Andrew, your line is open.

ANDREW>> Good morning, team. A couple of questions from me as well. First of all, you talk very much as if currently under the existing contract there is no opportunity for NZAS to extend. Do you expect them to come back in a couple of years' time and expect them to stick around a bit longer and how would you approach things if that did take place?

NEAL>> Yes, Andrew, they certainly have shown a tendency to want to re-negotiate contract terms over time, so it's entirely possible that they will approach us and want to extend, but what we want to try to make clear is that they don't have any contractual right to do so. So if we were to engage in or entertain such a thought, it would be because that was our next best option and we think we are working on some stronger potential options than that at the moment. Yep, they are more likely to want to engage at some point, particularly if aluminium prices hold up the way they are. It is a very profitable smelter now, but the optionality from their point of view is gone at this point.

ANDREW>> OK. Second question and it kind of relates to some of the things you were talking about around the fourth measure, am I right in effectively saying that they are not going to be spending the Capex refurb work and that if that pot line falls over they can force majeure on that? Or are you expecting them to spend that Capex?

NEAL>> Well, just one angle on this, Andrew. A technical or plant failure due to poor maintenance does not constitute a force majeure event in our opinion, but that's of course where you start getting lawyers involved and we've had experience with that. It was about 10 years ago when a transformer at the site failed and they lost a pot line. They ended up getting settled, that particular issue. That doesn't constitute a force majeure in our view, and we would fully expect them to maintain the asset in the way that it's sensibly operational for the next four years. Mike, do you have anything?

MIKE>> No

ANDREW>> So there was work expected to be some on the pot line, with Capex on that, you expect that effectively to go ahead?

NEAL>> Yes, if it's required to keep the plant operationally safely over the next four years, then it should absolutely go ahead and we would expect it to do so.

ANDREW>> The last question I had was around hydrogen and the site. People have talked about hydrogen as the great thing to be doing at the smelter site. Is that a requirement from your perspective or would there be other local sites that would work equally well?

NEAL>> No, it is not a requirement it is just the site has some existing facility that you might require off the smelter. There is nothing inherently fantastic about the site - I mean, it is close to the port. There is some existing infrastructure, Andrew, that a new hydrogen facility might be able to avail itself of, but time is also of the essence, and whilst the smelter is operational, it is taking up that space, so we'll see how it plays out.

ANDREW>> OK. That's all from me, thanks.

NEAL>> Thanks, Andrew.

ANNOUNCER>> The next question is from Peter Wakeman. Peter, your line is open.

PETER>> Thank you. Two questions: The first question is I heard you mentioning the forward contracts on the ASX regarding - not the ASX, the price, and you didn't say that you saw the significance - or someone said that. What do you think is of effect with wholesale prices when an announcement is made, say, closing the smelter and then a contract continuing it, from an earnings point of view for Meridian?

NEAL>> Peter, I think Mike is the best person to handle that one.

MIKE>> Yes, Peter, my reference was back in July, we had on the investor call back then and in our presentation noted that we have made some sales on ASX to help us manage the risk should NZAS provide us with a termination notice, and they eventually did in July. So that was my reference back then, and my reference to they seemed more important then could the smelter consumption be gone 2021, seemed reasonably important at that point. Obviously the smelter consumption will stay around to 2024, so those sales aren't as important as we thought they were back in July. That was really my reference there. Wholesale price forecast – I'd just be wrong, Peter, if I gave any form of wholesale price forecast. The only reference that we do have really is again back in July and after NZAS provided that notice of termination that wholesale prices did fall on ASX, but the ASX prices fell between $20 and $30 a megawatt hour on that notice, and have since risen. That is as good as a proxy I can give you, but trying to provide a forecast, I would be just wrong, Peter, as wrong as the next person.

PETER>> OK. The next question regarding other possibilities evaluating Meridian's portfolio. Is there any benefit of using the water from say Manapori for water bottling or tankers or something like that?

NEAL>> Peter, look, as I understand it, that has been looked at by different parties over the years, and I think what you're referring to is a large amount of water that gets discharged from the Manapōuri power station into Deep Cove and if that fresh water could be harnessed and used somehow, that would be potentially a value enhancing opportunity. We personally wouldn't engage in that. It is not part of our core business, and there are environmental concerns and issues with bringing large ships into that national heritage site to collect that resource, so that would be probably the sticking point in terms of getting anything up and going on that. But we personally would not engage in that as a business model: I should never say never, of course, but...

PETER>> Thank you. And the next question to do with electric ships.

NEAL>> Well, the world is changing at a rapid rate, so...

PETER>> Thank you very much.

ANNOUNCER>> Our next question is from Cameron Barker. Cameron, your line is open.

CAMERON>> Hi, guys. Firstly, congratulations a good result. Excellent for the market. One question really and that's just on the swaption in terms of alternatives. Mike, you've mentioned you will be looking at alternatives. Can you give us a flavour of time-frames, what sort of alternatives are out there, and does this mean that the current form of swaption with Genesis will be expired and not renewed?

MIKE>> Cameron, thanks, good question. Hey, look, I will answer the last part first: We don't know whether it be will be renewed or not. Obviously we will have an ongoing conversation with Genesis, but we don't have a specific answer as for when we will re-engage. We will pick that up in the next couple of days. I think as Owen opened the call, he said I'm still kind of on holiday, campervanning around the country, so we will reconnect with various people involved and work out the process moving forward. But one thing we did say on a previous call, was that we were exploring the options with a number of counterparties and we think we said - I could be wrong so I narrowed it in a little bit - but three or four counterparts that were willing and able to provide us with a form of optionality that will help us deal with that dry-year risk, and again today, one that I mentioned which would be a change in approach, was utilisation of energies from the likes of a new energy source like Harapaki to change the way that we ran our lakes which would then be in turn help usmanage the hydrology risks. So we have a few options. Obviously we are limited by the expiry date and anyone who had built anything would need us to move forward reasonably quickly, but it's recommencing aprocess that we kicked off way back in 2018, Cameron.

CAMERON>> That's great. Thanks, Mike. Nothing more from me. Thanks, guys.

NEAL>> Thanks, Cameron.

ANNOUNCER>>No further questions at this time. I would like to hand back to Neal for any further remarks.

NEAL>> OK. Thank you all. We did delay this investor briefing by a couple of days to allow a few more of you to get back to work, so hopefully that was helpful. Clearly there is further news to follow at our interim result announcement which will be on 24 February. Look forward to talking to you all then. In the meantime, have a good rest of the week. Thank you very much. Bye.