



TCNZ Finance Limited

Half Year Report

For the six months ended 31 December 2011

Directors' report

for the six months ended 31 December 2011

TCNZ Finance Limited ('TCNZ Finance') is a wholly-owned subsidiary of Telecom Corporation of New Zealand Limited ('Telecom') and is the principal finance company for the Telecom group. TCNZ Finance was incorporated in 1991, established an Australian branch in 2001 and a Bermudian branch in 2004. These branches closed their operations in the period ended 31 December 2011 as part of a group restructure following Telecom's demerger of Chorus ('demerger').

TCNZ Finance raises debt funding in New Zealand and internationally. The majority of these funds are then advanced to other members of the Telecom group in order to assist in funding their operations. TCNZ Finance enters into derivative financial instruments in order to manage the foreign exchange and interest rate risk associated with its borrowings, as well as to manage the foreign exchange risk associated with the operations of the Telecom group.

TCNZ Finance recorded a net loss for the six months ended 31 December 2011 of \$465 million compared to a net profit of \$261 million for the six months ended 31 December 2010. The majority of the loss related to debt forgiveness of \$546 million of debentures and other loans from a fellow subsidiary. Volatility in earnings is also caused by TCNZ Finance's exposure to movements in foreign exchange rates on derivative financial instruments that are held on behalf of the Telecom group. Additionally, \$170 million of the current period's loss arose from a debt restructuring following demerger, which gave rise to the novation of part of the company's pounds sterling, (GBP) notes outstanding, repayment of Swiss francs (CHF), Canadian dollars (CAD) and US dollars (USD) notes and closure of the associated derivatives. The net foreign exchange gain for the six months ended 31 December 2011 was \$89 million, compared to a net gain of \$162 million for the six months ended 31 December 2010.


The directors of TCNZ Finance consider the results of the company to be satisfactory and the company to be in a sound financial position.

TCNZ Finance solely lends to other companies within the Telecom group and accordingly, its financial performance should be considered in conjunction with the financial performance of the Telecom group. A copy of the Telecom group's results can be found at <http://investor.telecom.co.nz> or a copy can be requested from the registered office of TCNZ Finance.

On behalf of the Board



John van Woerkom
Director



Mark Laing
Director

27 February 2012

Directors' report

for the six months ended 31 December 2011

Declaration pursuant to Article 3 (2) (c) of the Transparency Law dated 11 January 2008

We, Mr John van Woerkom and Mr Mark Laing, both Directors of TCNZ Finance (herein after the 'Issuer'), hereby declare that, to the best of our knowledge, the condensed financial statements for the period ended 31 December 2011, which have been prepared in accordance with New Zealand equivalents to International Financial Reporting Standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Issuer and that the Directors' report includes a fair review of the development and performance of the business and the position of the Issuer, together with a description of the principal risks and uncertainties that the Issuer faces.



John van Woerkom
Director



Mark Laing
Director

27 February 2012

Income Statement

For the six months ended 31 December 2011

	Notes	Six months ended 31 December		Year ended 30 June
		2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
Finance income	2	445	448	902
Finance expense	2	(274)	(321)	(648)
Net finance income		171	127	254
Other income and gains	3	78	182	132
Other expenses	3	-	(13)	(12)
Debt restructuring costs	5	(170)	-	-
Fellow subsidiary debt forgiveness	6	(546)	-	-
Net earnings/(loss) before income tax		(467)	296	374
Income tax benefit/(expense)		2	(35)	(71)
Net earnings/(loss) for the period		(465)	261	303

Statement of Comprehensive Income

For the six months ended 31 December 2011

	Six months ended 31 December		Year ended 30 June
	2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
Net earnings/(loss) for the period	(465)	261	303
Other comprehensive income			
Translation of foreign branches	(28)	(5)	(2)
Cash flow hedges	62	(23)	(44)
Income tax relating to components of other comprehensive income	(17)	25	25
Other comprehensive income/(loss) for the period, net of tax	17	(3)	(21)
Total comprehensive income/(loss) for the period	(448)	258	282

The accompanying notes form part of and are to be read in conjunction with these financial statements.

Statement of Changes in Equity

For the six months ended 31 December

Unaudited	Contributed capital Number (m)	Contributed capital \$m	Retained earnings \$m	Hedging reserve \$m	Foreign currency translation reserve \$m	Total equity \$m
Balance as at 1 July 2010	883	883	646	(21)	18	1,526
Net earnings/(loss) for the period	-	-	261	-	-	261
Other comprehensive income for the year	-	-	-	(16)	13	(3)
Total recognised income and expenses	-	-	261	(16)	13	258
Balance as at 31 December 2010	883	883	907	(37)	31	1,784

Unaudited	Contributed capital Number (m)	Contributed capital \$m	Retained earnings \$m	Hedging reserve \$m	Foreign currency translation reserve \$m	Total equity \$m
Balance as at 1 July 2011	883	883	949	(52)	28	1,808
Net earnings/(loss) for the period	-	-	(465)	-	-	(465)
Other comprehensive income for the year	-	-	-	45	(28)	17
Total recognised income and expenses	-	-	(465)	45	(28)	(448)
Balance as at 31 December 2011	883	883	484	(7)	-	1,360

Audited	Contributed capital Number (m)	Contributed capital \$m	Retained earnings \$m	Hedging reserve \$m	Foreign currency translation reserve \$m	Total equity \$m
Balance as at 1 July 2010	883	883	646	(21)	18	1,526
Net earnings/(loss) for the period	-	-	303	-	-	303
Other comprehensive income for the year	-	-	-	(31)	10	(21)
Total recognised income and expenses	-	-	303	(31)	10	282
Balance as at 30 June 2011	883	883	949	(52)	28	1,808

The accompanying notes form part of and are to be read in conjunction with these financial statements.

Statement of Financial Position

As at 31 December 2011

	Note	31 December		30 June
		2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
ASSETS				
Current assets:				
Cash		119	53	207
Collateral funds		-	44	110
Due from other Telecom group companies		740	2,263	2,269
Short-term derivative assets		7	19	15
Total current assets		866	2,379	2,601
Non-current assets:				
Deferred tax asset		17	14	25
Due from other Telecom group companies		9,791	11,520	11,430
Long-term derivative assets		17	118	132
Investments		540	540	540
Total non-current assets		10,365	12,192	12,127
Total assets		11,231	14,571	14,728
LIABILITIES AND EQUITY				
Current liabilities:				
Income tax payable		14	6	26
Due to other Telecom group companies		8,769	9,797	10,099
Short-term derivative liabilities		15	328	334
Debt due within one year	7	420	613	397
Accrued interest		12	37	35
Total current liabilities		9,230	10,781	10,891
Non-current liabilities:				
Long-term derivative liabilities		23	286	329
Long-term debt	7	618	1,720	1,700
Total non-current liabilities		641	2,006	2,029
Total liabilities		9,871	12,787	12,920
Equity:				
Share capital		883	883	883
Reserves		(7)	(6)	(24)
Retained earnings		484	907	949
Total equity		1,360	1,784	1,808
Total liabilities and equity		11,231	14,571	14,728

On behalf of the Board of TCNZ Finance Limited



John van Woerkom
Director



Mark Laing
Director

Authorised for issue on 27 February 2012

The accompanying notes form part of and are to be read in conjunction with these financial statements.

Statement of Cash flow

For the six months ended 31 December 2011

		Six months ended 31 December		Year ended 30 June
	Note	2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
Cash flows from operating activities				
Interest income		445	448	902
Interest paid on debt		(297)	(317)	(640)
Net cash flows from operating activities	8	148	131	262
Cash flows from investing activities				
Net advances to/(from) other Telecom group companies		769	(330)	(40)
Cash flow on foreign exchange contracts		-	(10)	-
Payments on settlement of forward exchange contracts		-	-	(13)
Receipts from settlement of forward exchange contracts		-	-	2
Net cash flows applied to investing activities		769	(340)	(51)
Cash flows from financing activities				
(Increase)/decrease in collateral funds		110	(44)	(89)
Debt restructuring costs ¹		(211)	-	-
Proceeds from derivatives ²		1,000	-	-
Repayment of derivatives ²		(1,279)	-	-
Repayment of long-term debt		(961)	(15)	(28)
Proceeds from/(repayment of) short-term debt, net		336	106	(86)
Net cash flows applied to financing activities		(1,005)	47	(203)
Net cash flow		(88)	(162)	8
Net cash at beginning of period		207	216	195
Foreign exchange movement		-	(1)	4
Net cash position at end of period		119	53	207

¹ Excludes an accounting gain of \$101 million realised on derivatives novated to Chorus rather than settled in cash.

² The proceeds and repayment of derivatives relates to the cash flows arising from closing out hedges on the Telecom group's borrowings as a result of debt repayments.

The accompanying notes form part of and are to be read in conjunction with these financial statements.

Notes to the Financial Statements

For the six months ended 31 December 2011

Note 1 Financial Statements

These condensed financial statements of TCNZ Finance have been prepared in accordance with New Zealand Equivalent to International Accounting Standard ('NZ IAS') No.34: 'Interim Financial Reporting', issued by the New Zealand Institute of Chartered Accountants. In complying with New Zealand Equivalents to International Financial Reporting Standards ('NZ IFRS') TCNZ Finance is in compliance with International Financial Reporting Standards ('IFRS').

The condensed financial statements for the six months ended 31 December 2011 and 31 December 2010 are unaudited. The financial information for the year ended 30 June 2011 has been extracted from the audited financial statements of TCNZ Finance.

TCNZ Finance is a profit-oriented company and was incorporated in New Zealand on 19 July 1991 in the name of Randori Holdings Limited as a wholly-owned subsidiary of Telecom Corporation of New Zealand Limited (the 'parent company'). Randori Holdings Limited changed its name to TCNZ Finance Limited effective from 18 September 1991 and re-registered under the Companies Act 1993 on 31 January 1997. TCNZ Finance Limited Australian Branch ('Australian Branch') was established in 2001 and in 2004 TCNZ Finance established TCNZ Finance Bermudian Branch ('Bermudian Branch'). In the period ended 31 December 2011 these branches closed their operations as a result of a group restructure as part of the demerger. These financial statements include the activities of TCNZ Finance, the Australian Branch and the Bermudian Branch (each up to the date of closure) and have been prepared in accordance with the Financial Reporting Act 1993, the Securities Act 1978 and the Securities Regulations 1983.

The principal activity of TCNZ Finance Limited is that of a finance company for the parent company and its subsidiaries (the 'Telecom group'). In these accounts the term fellow subsidiaries is used to describe other subsidiaries of the parent company.

Basis of preparation of data

These accounts have been prepared in accordance with NZ IFRS and in accordance with the accounting policies detailed in the Annual Report of TCNZ Finance for the year ended 30 June 2011, a copy of which is available at <http://investor.telecom.co.nz>.

The principal risks and uncertainties for TCNZ Finance relate to ongoing interest rate and foreign exchange rate movements; credit risk relating to external counterparties and for amounts due from other Telecom Group companies and equity risk for amounts invested.

There have been no changes in accounting policies during the period. All accounting policies have been applied on a consistent basis.

Interim management report

The third paragraph of the Directors' report and notes 5-7 below give an indication of important events that have occurred during the first six months of the financial year and their impact on the condensed financial statements.

The principal risks and uncertainties for TCNZ Finance for the remaining six months of the financial year relate to ongoing interest rate and foreign exchange rate movements; credit risk relating to external counterparties and for amounts due from other Telecom group companies and equity risk for amounts invested.

Notes to the Financial Statements

For the six months ended 31 December 2011

Note 2 Finance income and expense

	Six months ended 31 December		Year ended 30 June
	2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
Finance income:			
Interest income on loans to other Telecom group companies	443	446	897
Interest income from deposits	2	2	5
Total finance income	445	448	902
Finance expense:			
Finance expense on long-term debt:			
- European Medium Term Notes	63	79	157
- TeleBonds	20	21	41
Revaluation of interest rate derivatives	1	2	3
Interest expense on loans from other Telecom group companies	184	213	434
Other interest and finance expense	6	6	13
Total finance expense	274	321	648

Note 3 Other income and expenses

	Six months ended 31 December		Year ended 30 June
	2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
Other income:			
Net Foreign exchange gains	50	182	132
Gain on winding up of foreign operation	28	-	-
Total other income	78	182	132
Other expenses:			
Net Foreign exchange losses	-	12	11
Other operating expenses	-	1	1
Total other expenses	-	13	12

Administration costs, including audit fees for the period of \$15,500 (31 December 2010: \$13,894, 30 June 2011: \$26,399) have been recorded by a fellow subsidiary company.

No fees or other remuneration have been paid to the Directors by TCNZ Finance or any related party in respect of services provided by the Directors to TCNZ Finance.

Notes to the Financial Statements

For the six months ended 31 December 2011

Note 4 Segmental reporting

TCNZ Finance operates within one industry segment, operating solely to finance the Telecom group of companies.

Geographical segments

31 December 2011	New Zealand operations \$m	Australian operations \$m	Other operations \$m	Consolidated \$m
Unaudited				
Finance income	377	35	33	445
Net earnings/(loss) for the period	(599)	165	(31)	(465)
Total assets	11,098	46	87	11,231
Total liabilities	(9,777)	(46)	(48)	(9,871)

31 December 2010	New Zealand operations \$m	Australian operations \$m	Other operations \$m	Consolidated \$m
Unaudited				
Finance income	394	10	44	448
Net earnings/(loss) for the period	304	(45)	2	261
Total assets	12,347	1,177	1,047	14,571
Total liabilities	(10,529)	(1,283)	(975)	(12,787)

30 June 2011	New Zealand operations \$m	Australian operations \$m	Other operations \$m	Consolidated \$m
Audited				
Finance income	794	22	86	902
Net earnings/(loss) for the period	367	(68)	4	303
Total assets	11,136	1,131	2,461	14,728
Total liabilities	(9,263)	(1,266)	(2,391)	(12,920)

Note 5 Debt restructuring costs

In the six months ended 31 December 2011, as part of the demerger, TCNZ Finance incurred costs of \$170 million in relation to the novation or repayment of TCNZ Finance's GBP, CHF, and CAD bonds and associated derivatives. This \$170 million comprised \$36 million of economic financing costs, along with \$134 million of accounting costs being realised in closing out debt and derivative positions.

Note 6 Fellow subsidiary debt forgiveness

In the six months ended 31 December 2011, as part of TCNZ Finance's exit from its Australian operations, TCNZ Finance forgave \$546 million of debentures and other loans from a fellow subsidiary.

Notes to the Financial Statements

For the six months ended 31 December 2011

Note 7 Long-term debt

During the six months to 31 December 2011, TCNZ Finance repaid the US\$250 million, CA\$275 million and CHF200 million of its bonds, including the related derivatives.

As part of the demerger, TCNZ Finance bondholders elected to exchange GBP235 million (NZ\$625 million at hedged rates) of TCNZ Finance GBP EMTN bonds to Chorus GBP EMTN bonds, issued by Chorus under the Chorus EMTN Programme. Bondholders representing GBP40 million (NZ\$110 million at hedged rates) did not elect to exchange to Chorus bonds and consequently these bonds remain in TCNZ Finance. The related cross currency swaps were split, and partially novated to Chorus along with the exchanged bonds. Prior to demerger, the interest rate swaps relating to the TCNZ Finance GBP bonds were closed out. New interest rate swaps have since been entered into, hedging the GBP bonds that remain in TCNZ Finance.

TCNZ Finance continues to have short-term financing programmes in place; a US\$1 billion European Commercial Paper Programme, a NZ\$500 million Note Facility of which \$184 million of notes and \$235 million of European commercial paper have been issued (and remain outstanding) at 31 December 2011. In addition to the short-term financing programmes, TCNZ Finance has a committed stand-by facility of NZ\$700 million (30 June 2011: NZ\$700 million) which is undrawn at 31 December 2011. The A\$1.5 billion Short Term Note and Medium Term Note Programme was disestablished on the wind-up of TCNZ Finance's Australian branch.

	31 December		30 June
	2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
EMTN	80	1,509	1,468
TeleBonds	542	554	542
Short-term debt	419	276	93
Unamortised discount	(3)	(6)	(6)
Total Debt	1,038	2,333	2,097
Debt due within one year	420	613	397
Debt due greater than one year	618	1,720	1,700
Total Debt	1,038	2,333	2,097

Notes to the Financial Statements

For the six months ended 31 December 2011

Note 8 Reconciliation of net earnings to net cash flows from operating activities

	Six months ended 31 December		Year ended 30 June
	2011 Unaudited \$m	2010 Unaudited \$m	2011 Audited \$m
Net earnings/(loss)	(465)	261	303
<i>Adjustments to reconcile net earnings to net cash flows from operating activities</i>			
Amortisation of discount	2	2	6
Foreign exchange (gain)/loss	(78)	(162)	(115)
Revaluation of derivatives	-	(7)	(5)
Debt close-out costs included in financing cash flows (note 5)	170	-	-
Fellow subsidiary debt forgiveness (note 6)	546	-	-
Other	-	2	4
<i>Changes in assets and liabilities net of effects of non-cash and investing and financing activities</i>			
Increase/(decrease) in interest payable	(25)	-	(2)
Increase/(decrease) in current tax	(2)	35	71
Net cash flows from operating activities	148	131	262

Note 9 Net tangible assets per security

	31 December		30 June
	2011 Unaudited \$	2010 Unaudited \$	2011 Audited \$
Net tangible assets per security	1.54	2.02	2.05

Contact Information

Registered office

The registered office of TCNZ Finance is:

Level 2
Telecom Place
167 Victoria Street West
Auckland 1142

Enquiries

TeleBond holders with enquiries about transactions, changes of address or interest payments should contact:

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Enquiries about the operating and financial performance of TCNZ Finance or the Telecom group can be emailed to investor@telecom.co.nz or addressed to:

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