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PRESENTATION

Paul Reynolds - *Telecom New Zealand - CEO*

Good morning, and welcome to Telecom Place and welcome to Telecom's first half year results, since we have moved to half year reporting. Although of course it's only a quarter since the last time, so this once and once only you get a quarter, it's a little bit of a quarter insight as well.

So content and agenda for today, I'll cover key messages up front, a little bit of a walk through our products and before a synopsis of our business unit performance Nick will take us through the detail on the Group financials and I will round up with the usual on some of the public policy issues and on guidance.

So, key messages. So adjusted EBITDA of NZD868 million is down 0.5%, that's where we expect it to be and plan to be and it's a result of the strategy and the focus we are putting on cost out focus is offsetting some regulatory impacts and competitive price pressures in the market.

You know we face those same challenges as most players in the telecommunications industry today and the focus on operational excellence comes through these results and is holding up our earnings. I think you know I highlighted a very solid fixed line performance as you will see in a minute.

Access lines are steady, churn and lines are pretty much world class levels, which we are pleased about and we have focused on targeted growth. A solid mobile performance for the first quarter, ARPUs are up, perceptions are improving, and the base is up and all as planned and on the back of what's for us a big period over Christmas, a decent sales period.

IT Services, often an indicator of business confidence and we're seeing revenue growth of 10% in that area of the market. Our international part owned cable Southern Cross the dividend this period was NZD39 million versus NZD44 million in the half 1 last year. Adjusted NPAT is impacted by significant taxation increases and regulatory increases coming through this quarter so that is at NZD158 million and down and those TSO is the rural broadband initiative and some tax changes at the top 1,000 previous term coming through in this half.

Strong operational focus means that our CapEx guidance has improved. We expect this year to be coming in between NZD950 million and NZD1 billion as opposed to our previous NZD1 billion to NZD1.1 billion. I'll talk a little bit more about that and so we are pleased about that it certainly is driving a better cash outlook.

Of course UFB negotiations continue. I will talk a little bit about that but there is a limit for obvious reasons to what I can say. But our headline is that a strong operational focus throughout the business in every line of business is driving - a focus on operational excellence is driving improvements. Reduced failure costs, better outcomes for customers, lower cash demands therefore on the business and that's offsetting significantly higher tax and regulatory impacts on our earnings. That's the headline.

Just a waterfall chart of the movements since the same periods last year. We started, H1 '10 was NZD872 million on adjusted EBITDA. The TSO impact is a negative NZD27 million a fairly significant number. The AAPT consumer sale had a one off of NZD7 million and there was a difference in those Southern Cross numbers that I explained, NZD39 million versus NZD44 million I think, so NZD5 million down there.

It was NZD14 million up on supplier settlements and NZD21 million up on lower operating costs brings us in fairly flat to NZD868 million EBITDA for the half. CapEx we've talked about this track for three years now. We knew the peak would come in FY09 and it begins to come off and that's on the back of investments in fiber, investments in mobile and really huge investments in operational separation. We're coming off on track, actually a bit better than we expected and adjusted to NZD950 million to NZD1 billion for the year.

You know that's about the second half will not see the rise in expenditures that we saw in previous years. That's due to the phasing of projects and a decision on which projects to run with and indeed the costs of those projects. So we are very confident that we have got that area under good control and delivering a better cash position.

Strategy update - you know our strategy is about positioning Telecom for a UFB world for a fiber world. You know however discussions and negotiations turn out the industry structure in New Zealand is going to change really quite significantly as it is in many parts of the world.

So we, our internal (inaudible) line is Vision 2013. We're working extremely hard on a 3 year plan and it's a call to action to deliver a strategy and it's focused on building momentum and operating excellence. Really getting the efficiency and effectiveness of our operations into world class levels.

Through that getting better outcomes for customers, reducing costs and managing our capital program extremely well. So we have individual programs and products, our IT and other platforms and process excellence. You will see in these results some real deliverables from those activities.

Getting the right efficient operating model for the business, focus on free cashflow through capital intensity and a lot of embedded initiatives to deliver on that. You know we have revised the accountabilities and goals of Telecom people over the past few months to really focus on the outcomes we want here and in particular at the end of the day to drive some free cash number that we think will be attractive to the market.

We are on track to deliver NZD155 million of new gross cost-out in FY11 and we continue to focus and target the growth in mobile broadband and ICT. We'll take a look at some of those products then.

Access and calling is pretty interesting. You know total Access lines are actually up very slightly 9k in this period versus the same period last year. I think the underlying trend would be a decline of maybe around 1%, you know very significantly better than other markets around the world.

We think founded on the universal availability of free local calling in New Zealand. The Access line and the free local calling that goes with it is a very, very attractive proposition for customers and it means that fixed to mobile substitution is probably rather less than in other markets.

Customers are having both mobile and they are having fixed on the back of the free local calling benefits. We're cautious about that. You know now fixed to mobile is something that many analysts and the market analysts look at very closely. But so far New Zealand has bucked the trend and the key difference I think is the free local calling.

Of course within that the market is changing its shape and lines are shifting from Retail to Wholesale. So at the Retail level we are losing some of those lines, holding onto them at the Wholesale level. But at the Retail level if you look at it our churn is around 6%, again pretty much a world class level. We've made some dramatic improvements in churn over the past couple of years.

Of course the other thing in Access that we think about and plan towards is the increase in fiber access, fiber right to the premises. You know our colleagues in IVC estimate that the fiber access market in New Zealand is now growing at about 20% per annum, so there is going to be some significant activity already taking place in advance of the Government UFB program. You will see and hear activities in our Retail, Wholesale and Gen-i businesses to respond to that as well as in Chorus of course.

Calling revenues are under significantly more pressure, clearly price pressure is going on in there and we're seeing substitution between voice to email to mobile, text and voice etcetera. But you have seen this is flat, actually this whole path there is slight growth in total lines; world class churn levels at the Access level and an increased churn level at the Calling side. That's Access and Calling.

Broadband total market connections in New Zealand still growing at between 10% and 12%. Overall the market in New Zealand is penetrated by 60% to 65%. That still leaves room for growth. We would see international benchmarks sitting around maybe 7% penetration. So good market growth and still some penetration to come.

Now as we have explained in previous quarters Telecom's strategy is focused on value and margin in this area. We are not chasing every connection. We are certainly not chasing no margin for unprofitable connections. You know we are holding Retail share steady at about the target we suggested, 54% overall share of the market at Retail. Now over a million connections in total on Telecom's Broadband network.

LLU continues to grow as you will see in the Chorus section later and competition is pretty intense in those LLU areas and you'll see our Retail business and the big RSPs in New Zealand go very intense competition, street to street competition across New Zealand right now; a vibrant area of the market.

Another final point in your feature of this market in New Zealand is wholesale pricing. The wholesale pricing in the New Zealand market is based on retail minus construct which is retrospective. So depending on the data, the offers that are out there at the retail level in New Zealand is flowed through retrospectively to the wholesale charge. That creates some volatility in the wholesale pricing, significant volatility.

We have seen that and we expect that to continue, it's just a fact of the nature of the regulatory regime in this market.

So let's look at mobile. Overall the mobile market - the consumer market I guess are some barometer of consumer activity overall. We expected at the beginning of the year something like about 3% overall total market growth in mobile in New Zealand. It seems to be running actually around 1% and I think that's a combination of intense price competition, but also a feature I expect of rather less rebound in economic growth than we expected let's say six months ago. So we've seen 1% overall market growth in mobile as opposed to 3%.

Connection - Telecom's connections in the first half were up 21,000. Of course they were down last quarter, so in fact over the last quarter and the Christmas period we saw some pretty significant growth - a 42,000 connection growth in the Christmas quarter. We're pleased about that. We're starting to see the churn in post-paid has gone. It's really a growth in pre-paid and a significant increase in smart phones and driving data - voice and data. So ARPU is up as well.

Telecom ARPU is improving as we see people convert over to XT. There's a lot of room for growth here and we think that smart phones - the New Zealand market is a little bit behind Europe and the States - we see about 16% overall smart phone penetration and that's 30% in some of the richer markets. So I think we still have a way to go in smart phone penetration, and therefore data usage and potential for us to uplift.

Mobile revenues in total were down over H1 and the fundamental driver of that is last year, on the launch of XT, we had huge handsets fails, which are now coming through in the numbers this period, so that's the dominant issues that's going on in there.

IT services - as I said earlier, returning to growth. Cloud services are growing. Overall market growth - we're seeing 10% growth coming through in Gen-I against an NZ market growth of between 3% and 4%.

I have talked previously about the session rebasing pricing level. You know a lot of price pressure as we worked through the global downturn. We're seeing some of that price pressure come off and the overall performance is stabilizing, which is good to encourage investment in this market.

We find Gen-I remains very well positioned, and particularly with its suite of ready cloud products are going to be very important.

Other big features - a couple of features of the market to talk about - I think the one government purchasing policy is highly important. Clearly the government sector is a major driver in IT services and that leading to centralization and rationalizing of suppliers. For us it's an opportunity. It's an opportunity to bring our new services to the market and it's an opportunity to pick the right panthers to play our part in that transformation in government services.

The other feature I want to talk about in this area is consolidation. Historically IT services has been quite a fragmented market in New Zealand, but we have seen over the past year some consolidation of players. NTT for example bought Dimension Data and Datacraft purchased some local companies like Axon and Integral. So we're starting to get a few more sizeable players and I guess that will begin to shape the competitive dynamics as we go forward.

Gen-I IT services up 10% - that's New Zealand and Australia. EBITDA margin is good, but it's seasonal, and it's trending upwards overall. The growth opportunity is there in growing the share of our existing customers' wallet. Well they are present in most of the major customers in New Zealand and getting a bigger share of that market is where the opportunity lies.

Let's look at the lines of business. First EBITDA up NZD6 million for the half year; 26,300 kilometers of fiber optic now deployed by Chorus. Really excellent, and much of that on the back of their SPCN program. Steady growth in UCLL - 101 exchanges now on bundle and we're starting to see some growth in UCLL outside of the main metro areas in New Zealand.

I think though the big story for Chorus is how - you know we've talked about operational excellence, how operational excellence improvements (inaudible) through in their numbers. For example we revised the contracts we have with their field engineering and service companies just over a year ago and the result of that is we're seeing a 15% improvement in meeting customers restoration and provisioning targets, so customers are getting a better deal. The (inaudible) get there on time and do a quality job better.

We have one third reduction in repeat faults. So we're getting there on time, we're fixing it right first time, and that's much better for customers and for the business overall. In fact the Right First Time initiative across Telecom and with our wholesale customers has resulted in around about 50,000 truck rolls per annum now coming out of the system. So 50,000 fewer wasted visits if you like that we don't need to do for customers. I think all good. It's a good example of operational excellence.

Next half plan for Chorus - clearly ongoing involvement with government in Crown Fibre Holdings on UFC and the RBI initiatives. Completing the FTTN program over the rest of this year. We've got 1000 cabinets to go, but every milestone on time - bang on time, like shelling peas - and we're very pleased. You know, as I said many things before about the project management and delivery in this part of our activities.

I think there are more cost savings to go in truck rolls and eliminating those wasted visits and improving customer service.

Wholesale and international - I mean we talked about broadband price volatility and you see some of that coming through in these numbers. External EBITDA - representing the wholesale's growth in the market is a growing part of our business - is up 9% on a like-for-like basis versus Half 1 the previous year. The fully traded EBITDA reflects our internal cost allocation and product mix - is down 58%. I think the 9% is the headline number and is a true reflection of the growth in the business. Access and broadband connections are growing strongly. We're clearly holding on to access lines and doing very well in broadband and keeping business in the Telecom Group.

Wholesale guys have a significant part of the operational separation undertakings that we're still working through. There were some biggies coming through in December 2010 and all met fully, on time, and in full, on our obligations to government there.

Next half I think significant focus on driving further customer service improvement. We think getting it right first time is good for everybody - good for the industry, good for the end customer, good for removing costs from the business - so cost containment.

Some new pricing offers of course and we'll reveal them when we're ready to reveal, and we continue in this part of the business to examine the international voice business. We're having good international voice business - the IVB world is a part of the market where business is consolidated and prices have collapsed significantly. So we have been in a strategic review for a few months and you'll see us come out with a new plan in the next half for that part of the business. A well run part of the business.

Retail - probably the biggest optics out there. EBITDA is up 36% on the same period last year. Good performance in retail in cost outs and of course a big part of that though is driven by the difference in cost of sales compared to the first half last year when we launched XT. Also retail enjoy some of the lower prices transferred through from wholesale as a result of that price volatility that I talked about earlier.

So cost of sales, wholesale pricing and strong internal cost control and control of head count all combining to deliver a very credible plus 36 on EBITDA in the retail business.

The churn in fixed line - as I say I think we are at world class levels. You know we're lasering down to sub-markets and in the SME market I think we've improved churn from 10%, 6% over about the last year as a result of some of the plan changes on our sales and marketing approach that I described in earlier quarters. So it's good to see some of those plans really delivering through to the front end of the business.

I think the little orange blob in the chart just is worth mentioning - it's really some months ago now - but we have replaced a product we called Big Time which was unlimited bandwidth with some very high bandwidth products launched in the market recently, but there was a churn at the time - three months ago - as a result of Big Time. It was a focused and rational business decision that we took, but we thought we'd show you it as part of the churn numbers and it will wash through the system now as we go forward. That's behind us, and incidentally the new plans that you have just begun to see on the telly and in the market have been going strong so far, so we're expecting good things to report next time.

One of the big issues for retail - one of the big areas to focus on is mobile. What's coming through very clearly in the market in our customer satisfaction and our comparative statistics is that the network's superiority of the XT product - which we have known about in engineering terms - is really coming through anecdotally in customer perceptions and customer statistics. So clearly we have to leverage that now into even better sales growth. We saw it come through at the Christmas period and so the retail business very very focused on leveraging superior XT performance. You will see further refresh of our mobile plans in the next period.

Smart phones are a big part of that. As I was explaining earlier, smart phone penetration in New Zealand is comparatively low and the more smart phones are there the more application services and data people are using - whether it's for Facebook or LinkedIn or (inaudible) community or whatever that's up on the web - so I think an exciting part of the market and a lot to go for.

I talked about those new broadband bundles. We expect that to go well. I think another thing just to finish on in retail is we are moving very fast towards a fiber based world and a part of the development process is looking at fiber to the node product which we will be integrating as the new wholesale part of these services become available. In the meantime there'll be an unrelenting focus in operational improvement, operational excellence, getting it right for customers first time and getting across that business. (Inaudible) EBITDA growth of 6% over H1 and IP services EBITDA and you know we've focused very hard on this, making sure that the EBITDA margin and IP services right is up 15% on comparative period. As I said earlier the price decline in voice data, we said the reset - the one off reset that we saw during the global financial crisis, we've seen that flatten out. It's a more competitive market, a sharper market than it's ever been and we see in these numbers that Gen-i is more than up for it and able to compete with every other player in the market. Again, an increased focus on fiber based services, built and ready and currently selling as we anticipate a much increased demand for fiber based services and a USB role. Mobile's going good, 5% connection growth half year up. You're really in a very, very significant share of the enterprise and Government market in New Zealand on the back of that superior proposition and XT.

Australian revenues you'll see down in this period. We decided not to renew the CBA contract in Australia - Commonwealth Bank contract in Australia back in I think 2008, Chris wasn't it? In fact, the customer has stayed with us for a significantly longer period than was anticipated, which is good news. That transition to the new supplier has begun to kick in over the past months and you're seeing some revenues come out, which probably we expected last year actually, so just explains with what's going on there.

One for next time - I mean our unrelenting focus on IP services margin and to operational excellence that are very well structured to the program on operational excellence in the Gen-i business. We fully expect that to continue and improve margin performance as we go forward. I mean, just as an example of that, we've identified about 200 services that we domestically will simplify. That means eliminate systems so we'll not incurring the costs in (inaudible) stuff that is not a priority for customers. We've done 66 of those already and that's an energetic and ongoing program. Further cost out through suppliers, get overheads down, Right First Time. The opportunities to grow still remain in mobile and cloud services and really cementing our Trans-Tasman piece. I think you're going to see a lot of operational change in the next period as we leverage for our Trans-Tasman clients who operate in both Australia and New Zealand on common platforms, common processes and we do it really well and really efficiently so that they get a quite similar services, the same feel and look from Telecom Gen-i whether they're here in New Zealand or in Australia. We will over the next period complete the CBA migration.

Finally on a walkthrough of the business units, AAPT, the first part EBITDA was NZD38 million and impacted (inaudible) we sold the consumer business as you know and they've received I think NZD176 million in New Zealand dollar proceeds from that and that would include the stakes in iiNet and Macquarie Telecom, which were related to transactions, NZD176 million received. But of course that takes some volume out of the business and wholesale contracts we had with Telstra are commercially negotiated but volume related. So some of that discount went out from the back of the bill and you see that coming through in the results. As ever, a strong OpEx and efficiency performance from the AAPT team and that is lowering OpEx and partly offsetting the pressures that were seen on the EBITDA line. Strong sales performance. This is a business B2B and wholesale business, a good fiber network. We have in fact completed a significant upgrade of our Australian intercity fiber network through this period. We can connect all the key centers and that's a big plus for corporate and government clients. In the last year, some big wins with Exetel (inaudible), Brambles and several others. Our sales focus for the next half is in new wave products and AAPT it's SIP products, and on data and a big push to complete the consumer transaction. You know when you dispose of some part of the business it actually costs less than the business it's behind, so removing those related costs is a big part of the focus.

People have asked us about the floods in Queensland. I think a good customer service response from the boys and girls in AAPT, they think it has received minimal impact, certainly minimal impact for customers, I think low international terms that we will complete our analysis of that over the next few weeks. We will finish I think in this period the billing rationalization program that we've been running through AAPT for the past significant number of quarters and that's a big, big one, a much simplified the operating process for the business.

So that's the run through, operational excellence. Significant gains in that area in each of the lines of business, offsetting increased tax and increased regulatory demands that keep running in a stable path and following guidance.

Nick Olson *- Telecom New Zealand - CFO*

Thanks Paul. I'm going to kick off with a summary of the key financial metrics. As Paul has said, adjusted EBITDA of NZD868 million was down NZD4 million or 0.5%. There were a number of one off items that we have not adjusted for. The largest negative impact of NZD27 million of regulatory downside in the half relating to TSO and RBI. We have highlighted this before and it relates to the loss of TSO revenues and the impact of funding the Government's Rural Broadband Initiative. AAPT's EBITDA has declined, of which NZD7m was due to the sale of the Consumer division. The timing of the sale and associated stranded costs mean that EBITDA for AAPT is expected to be lower in the second half. The Southern Cross dividend of NZD39 million was NZD5 million lower than the corresponding half last year, but this was more than offset by NZD14m of Supplier settlements.

These impacts were partially stemmed by a continued focus on cost out and a lower level of costs of sales, which resulted in a net NZD21 million positive impact such that the overall decline on adjusted EBITDA was only NZD4 million. These reductions also keep us on track to deliver our gross cost out target of NZD155 million this year. I also wanted to highlight the changes in head count as there are some solid trends emerging. IT Services head count grew 4% reflecting revenue growth, support head count in T&SS and Corporate fell 1% and head count in the business units, excluding the sale of AAPT Consumer, fell 5% compared to the first half last year. These reductions have allowed us to reduce overall labor costs by almost 4%.

In the second half there will be a fairly significant increase in our head count as we bring 325 employees in house from our outsource partner HP/EDS. As a result, our employee costs will increase, but our direct costs are expected to decrease. We expect a small saving this year from this activity and most importantly, you can expect real management focus on underlying head count going forward. We have also announced a Q2 dividend of NZD0.3.5, which will be fully imputed. Just to remind everybody we continue to pay dividends on a quarterly basis, not half yearly basis.

In terms of the reported income statement there are several adjusting items which may distort the underlying performance, so we'll skip quickly to the adjusted income statement over the next page. The first adjusting item was an NZD18m gain on the sale relating to AAPT Consumer. We have also taken a decision to treat UFB and earthquake costs of NZD12 million and NZD4 million respectively as adjusting items for the half year. At the Q1 result these items were not treated as adjusting items, but we now believe they are of such a size, that any other treatment would distort the true performance of the business. The tax effect of these items is NZD5 million. We have not yet made any allowance for the costs of the flooding in Australia, although our initial assessment indicates that no significant damage has been sustained.

Now moving onto the Adjusted Income Statement, revenue declined by 3.3% to NZD2.6 billion relative to the first half last year. The NZD88 million decline was mainly in access and calling as competition impacted the business. The sale of the AAPT Consumer division is also reflected in the numbers. Revenue growth in IT Services was offset by other reductions in mobile and data revenues. Expenses for the half year decreased by 5% to NZD1.7 billion. The decline of NZD84 million was primarily in other operating expenses and reflects lower mobile cost of sales due to strong XT handset sales in the prior period and ongoing cost out activity. Labor costs were down 3.9% reflecting continued cost and headcount reduction initiatives. Depreciation and amortization increased by NZD20 million to NZD530 million as a result of the higher overall asset base and a reduction in some asset lives. Tax expense was NZD58 million higher than the previous half year mainly due to a NZD43 million credit recorded in the first half of last year and an additional NZD23 million expense recognized in the first half of this year, as a result of one off changes to tax legislation. Both of these changes were signaled at Q1. Adjusted net earnings were 35% or NZD85 million lower than in the first half of FY10. This was driven by the increase in tax expense, financing and depreciation and amortization.

Looking now at the EBITDA for each business unit. The biggest movements this half are falls in EBITDA in Wholesale and International, which Paul has covered and AAPT and an increase in EBITDA for Retail. The Wholesale and International decline was driven primarily by decreased internal revenues due to changes in UBA broadband pricing, data and international bandwidth pricing. Wholesale & International also made greater payments to Chorus due to Chorus' deployment of FTTN cabinets, and growth in the volume of fixed lines.

It is worth noting that external EBITDA of the Wholesale & International business continues to increase. The decline in AAPT's EBITDA reflects the sale of its Consumer division, lower volumes in Wholesale and Business and the effect of increased wholesale inputs.

The increase in Retail EBITDA was largely driven by reduced payments to Wholesale as internally traded prices fell, lower mobile cost of sales and advertising costs.

Looking now at the cashflow statement for the first half. Operating cashflows were NZD285m lower than the prior period. This was due to an NZD86 million increase in tax payments, NZD50 million increase in inventory purchases, and NZD43m of TSO receipts in the prior comparative period and not repeated in this year.

The impact of the consumer sale by AAPT, slightly negative revenue trends and some other working capital requirements So overall, this large change was a combination of a particularly strong first half last year, and a relatively weaker first half in this year. Investing cashflows were NZD154 million better than the NZD574 million invested in the first half of last year, largely due to NZD176 million of proceeds received from the sale of the AAPT Consumer division and stakes in iiNet and Macquarie Telecom.

Cash applied to financing was NZD90 million as we paid dividends of NZD177 million which was partially offset by a small increase in debt.

As Paul has said, we have had a laser-like focus on improving free cashflow this half. CapEx is one of the most effective levers we have to improve free cash flow generation and we have aligned staff incentives to ensure a Group-wide focus on our free cash flow targets.

We now expect to spend between NZD950 million and NZD1 billion on CapEx this year. This change in guidance is the direct result of a thorough review of every material item of CapEx in plan. In fact 145 projects were reviewed by business units and a central committee.

The review challenged business units to reduce spend in low growth markets, re-validate investment needs and take tight control of project costs. Delegated financial authority limits were also revised in December to help manage and mitigate incremental spend. Overall the reduction in CapEx is the result of incremental savings across all projects, not just cutting the big ones, reflecting the detailed nature of this intervention.

CapEx was NZD480 million the first half or NZD20 million than in the first half of FY10. But the key takeaway is that we will actively manage run-rate over the remainder of the year. At a detailed level, spend on the Transformation and Regulation program decreased by NZD56 million.

The biggest reductions were in FNT, which was NZD35 million lower as core capability development nears completion, and in separation as the majority of separation commitments have already been delivered. These decreases were offset by a NZD34 million increase in XT mobile network capacity in line with our forecast to meet demand.

Business sustaining CapEx was NZD36 million higher than the prior comparative period, and Chorus continues to maintain tight control of the FTTN programmer and other project spend.

Finally, let's take a quick look at the financial profile and capital structure. Net debt for the first half increased slightly due to weaker operating cashflows. We maintained our credit ratings with S&P at single A, credit watch negative, and with Moody's at A3, stable outlook. As per our dividend policy we have declared a Q2 dividend of NZD0.35 cents per share. The dividend will be fully imputed at a ratio of 30 over 70.

In addition, a supplementary dividend of NZD0.62 cents per share will be payable to shareholders who are not resident in NZ. Again, we have suspended the dividend re investment plan and on-market buy back due to the current status of UFB negotiations.

Looking forward we remain focused on maintaining an appropriate capital structure for the current operating environment which is heavily impacted by regulation, competitive pressures and of course the government's Ultra Fast Broadband initiative.

Thank you, back to you Paul.

Paul Reynolds - ***Telecom New Zealand - CEO***

Thanks, Nick. So we just round up before we go to the questions. On UFB of course we remain in discussion with Government, with Crown Fibre Holdings. There have been in the last year some significant industry workshops run by the MED and others as regards to the relationship, should we be chosen as a partner.

So that's been very constructive and I think you know cleared ideas for many people including ourselves. One thing that a lot of people do ask is, when construction operations will be done? Well that depends on when you start the process and that of course depends on the timing of striking any deals with CFH. So we would update, should we reach a deal, we would update the timetable on structural separation dates.

That means clearly structural separation is a simply gigantic and complex piece of work in both New Zealand and in global markets as we restructure the business and all the Company's financial arrangements. So it is a very significant and non-trivial exercise.

Rural Broadband Initiative, we are with Vodafone in discussions following the Governments' decision this week to take discussions forward with us on that. We are pleased with that and we will engage and I guess no doubt further news coming in the next few weeks.

In both initiatives, and of course a piece clearly, strategically we think getting the best outcome for New Zealand aligning with Government where we can and structuring a long term arrangement that will be good for Government, New Zealand and shareholders is our strategic objective and we work on that very hard and I think pretty professionally.

Overall in public policy and regulation, you know, I think in past sessions we have given very detailed chart by chart progress on the operational separation milestones. You know some of those -there are many still to go, but we are building a track record of success and delivering on time and in full and we continue to do that through to the last period.

I guess the other big thing in people's minds is mobile termination rates. The Commerce Commission's draft decision, as I think you know, signals to NZD0. 468. In the short term how this will impact on Telecom, that would be a small upside as we are clearly net outpayers, as everyone is to the biggest player in the market Vodafone.

In the longer run you know changes to termination rates can make the Retail pricing position more competitive, so I think there will be further price pressure in the market. So anyway the final decision is expected in late March and for our part we will be like to just get on with it.

The chart here I think that is hopefully helpful to you and you can peruse at your leisure. But as we talk about this area, clearly with a company that has so many strands of regulation and public policy affecting it, we have our thoughts, structured in a strategy and we're getting, we have talked about some important developments, positive developments for the Company and they are in here and some things that we still would like to see and we continue to argue for.

So this chart kind of sets out some of the headlines. You know you can go to 20 pages in this stuff because there is so much of it. But clearly we are trying to get the regulatory environment simplified, it's a burden for industry and overall. Being as simple as possible and targeted and proportionate is important.

Clearly a big objective is getting pricing that supports investment. You know we as an industry are one of the biggest investors in New Zealand in New Zealand infrastructure and that's got to be a good business to deal with. Not always at the minute and arguing and working towards pricing supports investment as a big part of strategy.

Of course getting to best practice governance arrangements in New Zealand is incredibly important. It's a very interventionist situation and there's not a lot of public debate or comeback as you see in other markets. So we will continue to argue for clear regulatory duties and objectives, accountabilities and the ability to error correct if something is done inappropriately.

So we don't argue for no regulations but we argue it should be right size, appropriate and have the sort of corrective mechanisms that we see in international markets and are absent in the New Zealand context.

We were pleased this half on the Commission's decision throwing back Resale regulation and we were also pleased with the draft decision to re-regulate bitstream in urban exchanges. Those decisions peel away some of that complexity and help us. We have also seem some flexibility we are pleased about as regards to the operational separation undertaken and Variation 3 and Variation 4 are sensible reactions to the ongoing development of technology and the market and ensuring that we build a strong and credible wholesale market structure in New Zealand.

Also in the period we've seen a decision on VDSL and the ability to differentially price for faster VDSL based products. Well that's a great intervention because why would you, what's the point of investment in faster, better if there is no ability to price a value price in the markets.

It's a great encouragement to us and I am sure others to get on with investing in the right place, hence this market. So some positive steps but there remains a lot to do. The separation model, the operational separation model that we came under at the beginning of 2008 is exceptionally complex and there is significant scope for simplification.

There is certainly significant scope for getting the appropriate rates of return recognized in pricing decisions so that the right WACC is reflected through. We have, and continue to argue, for a merit based review, the ability to error correct for regulatory decisions that might have taken the wrong angle.

You know we like the UK style duties which are reflected in other markets in regulation which is there was a bias against intervention overall; that there is an explicit need for a regulator to promote self-regulatory solutions where appropriate. There's a bias and a preference for least intrusive measures and a duty to look for opportunities to deregulate.

So, you know, summary overall - progress in some areas; work still to do, and there remains a very important area for us obviously.

I'll finish up on guidance. Adjusted EBITDA remains unchanged. It was between NZD1.72 billion and NZD1.78 billion, and that absorbs the impact of the AAPT Consumer sale within the range. Depreciation amortization remains at 1% to 1.06%. The effective tax rate around 53% and we are very pleased that the operational focus that is delivering an improved CapEx guidance of NZD950 million to NZD1 billion. Adjusted net earnings of between NZD330 million to NZD370million to complete the picture.

FY12/13 I won't read out the numbers, because it remains unchanged.

Thank you.

We'll go to questions. As usual with the room first and then we'll go to online.

QUESTION AND ANSWER

Tristan Joll - ***Goldman Sachs - Analyst***

Morning guys. Tristan Joll, Goldman Sachs. I've just got three I guess guidance related questions. Just on AAPT - that run rate and the impact of those hand costs looks slightly more severe than what I would have thought based on the guidance you gave at the time. I would have thought it was unduly stacked in the first half, but does your comment note that you'd expect it to be lower again in the second half? Can you sort of give some color on that?

Nick Olson - ***Telecom New Zealand - CFO***

yes, sure Tristan. Look I think the reality is actually there's a lot of competitive pressure on AAPT at the moment, so that's an element of it, but there are - the stranded costs are significant and the management team just needs time to work through those. It's a really significant exercise for them and as you know we back that team to the limit to actually deliver that, but it will take time.

Tristan Joll - ***Goldman Sachs - Analyst***

Okay. Then in terms of the CapEx stuff, could you give us some sort of idea how much deferral there is in there? So what I'm now thinking is...

Unidentified Company Representative

(Inaudible -- microphone inaccessible)

Tristan Joll - ***Goldman Sachs - Analyst***

Right, so would I expect to then extract that kind of run rate out of my CapEx spending over the next few years or - I guess what I'm trying to get to is how does this affect your path back to a normal level of CapEx?

Nick Olson - ***Telecom New Zealand - CFO***

Look, Tristan, you know I think there's a bit of a story here. Yes we have talked to the analyst community and the investors lots about our objectives to improve pre- ash flow and this to me delivers stage one. It's been very deliberate intervention and I think the message I would send to the market is the first part's the hardest because we've gone from a regime where we were forced to spend at a certain rate for regulatory reasons, so now we need to move to a stage of very very tight control.

So minimal deferrals. This is all about the right scoping, the right focus, alignment with strategy, insuring there's no duplication across the organization, appropriate challenge processes at all stages of project - pre-feasibility, feasibility - before work commences on projects. And we actually have a very very strong focus and team around ensuring that we minimize CapEx spend.

We're not going to give forward guidance on CapEx at the moment, but you know pre-cash flow is a measure by which I'm going to measure the market success and the organization success, so you can expect that our aim is to actually keep on repeating those sorts of results.

Tristan Joll - ***Goldman Sachs - Analyst***

Okay, and one last one, I just extending that into OpEx - I see the vision 2013 slide is interesting and the fact that you're on track for the 155 and committal cost-outs this year is also interesting. I suppose that target however was set back in '08 and I know it's been adjusted for some operating relatives since then, but does vision 2013 I guess consider the UFB in a greater light? I suppose what I'm trying to ask is are you going to seek to revise those cost-out targets upwards because of the UFB? Because at this point I think you've only really changed the operating relatives in the fact that there isn't enough growth in the business. Are there more cost-outs to come?

Paul Reynolds - ***Telecom New Zealand - CEO***

We're going to fish them as hard as we possibly can and clearly we're (inaudible) to drive pre-cash flow, which is what we're doing. I'm not going to give you more specific targets, but at this stage what we're saying is you guys had a lot of skepticism I think a year ago about our ability to drive operational improvement cost reduction. I think that's - we have fully vindicated the plans that we've gone for, so we've both in both the OpEx line and the CapEx line and we can see continued momentum within the business.

So I'd expect it to reflect through an increased confidence in your side that we are on track and can meet the sort of ambitious goals that we've set.

Nick Olson - ***Telecom New Zealand - CFO***

Yes, I think it's watch this place Tristan. I think your observations are good and that our focus is to do better.

Geoff Zame - ***Craigs Investment Partners,Deutsche Bank - Analyst***

Nick, Paul, hi. Geoff Zame, Craigs Investment Partners/Deutsche Bank. I just had a bits and pieces that I was interested in exploring. One probably just on a CapEx front - you know you obviously could see that focus on it, but in the context of the categories that you disclosed, perhaps a little bit more color on where you actually see more of the (inaudible) potentially?

Nick Olson - ***Telecom New Zealand - CFO***

Look, I think the reality Geoff is that regulatory CapEx will fall over time, so I think you guys can probably make an assessment as well as we can about how the regulatory CapEx will fall off, and that will be a big driver of downward pressure on CapEx. However we still very much have our sights set on improving overall efficiency of the CapEx spend.

There's several elements of that. It isn't just about the internal process. It's about aligning incentives. So you know effectively we have aligned our staff incentives with shareholder incentives. So the shareholders have told us pre-cash flow is the most important metric from their perspective and there is aligned incentive to do that.

So we've got process, we've got incentives - so the other piece of the equation is actually efficiency both internally in terms of delivering CapEx and with our partners. So I guess there's a term I have often used, but we've got to be careful not to suffer from death by invoice from our vendors.

So that's about giving visibility of where the spend is, making sure that actually our vendors are an early warning system as well in terms of overall CapEx spend, and making sure we scope projects correctly.

You know this is an engineering based organization and as an engineer myself, you know, you always want to build a bridge so it stands up forever, but there's a limit to that and there's a limit to what's optimal.

So it's about efficiency, optimal behaviors and optimal deliver from both us and partners.

Geoff Zame - ***Craigs Investment Partners,Deutsche Bank - Analyst***

This sort of brings me onto one of the next questions just around the whole supply settlements part of it. I mean the death by invoice from vendors is starting to write your checks. I mean is that something that's going to go on on perpetuity? I'm just trying to understand in the context of it's not split out as sort of a separate adjustable line item.

Paul Reynolds - ***Telecom New Zealand - CEO***

I think you would be wrong to think it's the end of the road. There are always adjustments from various suppliers, usually in a quarter-on-quarter period. But there's no guidance in here about putting on in perpetuity either.

Geoff Zame - ***Craigs Investment Partners,Deutsche Bank - Analyst***

Right. Just a couple of last ones - just on the mobile market, I mean Vodafone obviously came out with some pretty good numbers on the connection front, and you've had a pretty good Christmas quarter - can somebody in this business just give me a little bit of context on how you sort of see the market and how Two Degrees might be doing against that backdrop?

Paul Reynolds - ***Telecom New Zealand - CEO***

I don't think we could comment on Two Degrees in this period. I'm sure they'll let their numbers out in due course, but maybe Alan you want to talk about how the market feels right now?

Alan Gourdie - ***Telecom New Zealand Retail - CEO***

Hi Geoff. Yes, we had a good quarter, particularly the Christmas quarter, we saw that net add - somewhere about 40,000. I think what I was most encouraged by with that though was some of the high value smart phone device trends that we saw.

Paul mentioned the penetration that we have seen and the growth in our base of smart phone devices - around about I think 16%. That's our base. That's Telecom base. That's not the total market. Within Gen-i that was around 37% of their business is now smart phones and it's now about 12% for retail. Those businesses showing really significant improvements in those smart phone device penetration rates.

So that's a result of our Android strategy by and large. And you know what that's doing is it's starting to drive data, as you might expect, but interestingly also things like voice minutes and voice revenues are going up because people who have got these phones, they actually use them for all of the products on the device.

So we're very encouraged by that. It is turning into higher RPUs and with further penetration evident from those overseas trends - because by comparison we're relatively low, half of for example some markets in Europe - and in fact quite some way behind Australia, which I believe has a penetration somewhere around 50%. So if you start to factor in some of the trends that are driving our revenues from that and that gap, you can see the sort of opportunity that we're seeing, all based on the quality of the network now starting to come through very strongly. There is a significant gap in performance. Our customers are starting to report that and we're certainly looking to use that to drive things like that smart phone penetration.

Geoff Zame - ***Craigs Investment Partners,Deutsche Bank - Analyst***

Thanks Alan. Just to wrap, just on the UFB - there's quite a bit of depth sort of all over FY12. How are you thinking about that in the context of UFB and also just the other (inaudible) and your timeline thing - I appreciate it all depends on if and when you strike a Heads of Agreement with the government (inaudible), but assuming you do strike a Heads of Agreement at a certain point in time, you must have a project timeline to suggest the process to get to a structural separation of (inaudible) in place - six, eight, 10 months. Can you give us some sort of color on that?

Paul Reynolds - ***Telecom New Zealand - CEO***

I'll do that first and then maybe Nick can talk up the [debt]. I'm not going to give you any more Geoff, but suffice to say that as you know regional timetable was the government set was to have some decisions made before Christmas, and we made some predictions on the separation in the second half of the year based on that, so you're talking rough timetable. It's several months of course but we will name if called upon and if we do reach an agreement we'll name a separation timetable at the time. So you know how complex it is and many factors have to be taken into play, but it's a substantial program of work.

Nick Olson - ***Telecom New Zealand - CFO***

Geoffrey, what a great question and I think you've seen this before with your time at Telecom. The reality is actually said to be almost impossible for us to actually turn debt at the moment, because of the uncertainty of USB. But we have a number of banks that have already expressed a willingness to actually roll over debt that we need to deal with. I think December next year is luckier when we have a debt roll, so that's the reality of being in an uncertain process, so you can have information asymmetry and that will prevent you securing long term debts, but we've a very, very strong capital structure and very, very supportive bankers. So the risk of that of course is that we're just in time for the flurry of lunches from the banking industry, but we'll try and hold back.

Paul Reynolds - ***Telecom New Zealand - CEO***

Up the front here please.

Guy Hallwright - ***Forsyth Barr - Analyst***

Guy Hallwright, Forsyth Barr. Just following on again on the questions on XT, in that quarter XT or the mobile business in general had reasonable growth but it's in pre-paid not in contracts. Vodafone's growth in the December quarter was done in contracts and that tells me that there's still not really attraction there to the new network and making the business market. You're talking about (inaudible) and a relaunch (inaudible) there'll be more aggression in the marketplace. Can you just...

Paul Reynolds - ***Telecom New Zealand - CEO***

I mean, let me take it first. I think the corporates we've seen churned in the post-paid (inaudible), that's been eliminated. So the trend up - our ambition is for more clearly and we're pleased that the momentum's that begun to build in this quarter, it's not about the cycle that can also tend to grow a lot. On the business market, I mean I guess you mean SME business and the corporate market I think we're particularly pleased with and will reach. So a lot of focus going forward in this area as we think we're the best offer out there and that's - and the customer preference and satisfaction so that was a (inaudible) and that's what we'll build on going forward. Clearly we (inaudible) to growth in post-paid across the base. Alan, do you want to answer that at all?

Alan Gourdie - ***Telecom New Zealand Retail - CEO***

Not a lot Paul. I think to your points about Gen-i, Christmas has reminded me that 5% of his - the 5% growth that's all on account of course in his business. In our business, (inaudible) was particularly strong during the quarter, so to your point Paul, what we've seen through the half and particularly through the quarter was an elimination of the churn and then a steady growth in those post-paid numbers. Absolutely not what we're looking for. We're looking for much more growth in that area and with that network situation, with a very strong handset range now and with our plans being refreshed, it gives us a very strong voice text data bundle through our customers, we fully expect that momentum to continue.

Guy Hallwright - ***Forsyth Barr - Analyst***

Also just going back to AAPT following on from just your question I think it was, there was a NZD7 million impact on the loss of AAPT consumer in the quarter effectively (inaudible) quarter. The original guidance I think was for the impact of that to be NZD10 million annualized, which is NZD30 million (inaudible). You look to have done half of that in the first quarter. Is that NZD10 million Aussie annualized NPAT, was that perhaps understated, are you looking at more than that?

Nick Olson - ***Telecom New Zealand - CFO***

Yeah. I don't think that we had a strong enough fix on standard costs at that point.

Guy Hallwright - ***Forsyth Barr - Analyst***

Just to clarify when you mentioned lower AAPT in the second half, you were talking about lower accrual.

Nick Olson - ***Telecom New Zealand - CFO***

Yes, slightly lower overall.

Guy Hallwright - ***Forsyth Barr - Analyst***

Alright, thanks.

Paul Reynolds - ***Telecom New Zealand - CEO***

Another one. Questions online?

Operator

Thank you. We have four telephone questions, the first coming from Sameer Chopra of Merrill Lynch. Sameer, please go ahead.

Paul Reynolds - ***Telecom New Zealand - CEO***

Hi Sameer.

Sameer Chopra - ***Merrill Lynch - Analyst***

Good morning. I hope things are well. I had two questions. Firstly, if you look at the free cashflow trend that might be expected in the second half, you've given us color around CapEx and EBITDA. I was wondering if you can talk about what do you expect in terms of working capital. What usually happens in the second half, what are you expecting in the second half on working capital?

Nick Olson - ***Telecom New Zealand - CFO***

We were hoping to avoid these really detailed questions today, but look, I think from a working capital perspective we're actually doing a little better than we were last year. But the reality is that we're not going to end up larger in the last month of the year on CapEx and so we're not going to see the big reversal that we did going into the end of the year that we did last year.

Sameer Chopra - ***Merrill Lynch - Analyst***

Alright. Then the second one was - Paul, you mentioned that structural separation is at a significant and non-trivial. Are you talking about this from a time perspective or a cost and CapEx perspective?

Paul Reynolds - ***Telecom New Zealand - CEO***

My comment was specifically about the complexities and timeframe for it, but clearly depending on the nature of any agreement that a range of costs for structural separation should incur. I think a lot of that depends on the degree of which can be shared systems and the timeframes over which new businesses completely separate those systems. That's all the sort of stuff that was on in negotiation and is certainly the reason why I couldn't give you an estimate of it. But my comment actually today was about the complexity and timeframe.

Sameer Chopra - ***Merrill Lynch - Analyst***

Great, thanks. Thank you.

Operator

The next question comes from Richard Airey of UBS. Go ahead please Richard.

Paul Reynolds - ***Telecom New Zealand - CEO***

Hi Richard.

Richard Airey - ***UBS - Analyst***

Morning Paul, morning guys. Just a couple of questions. Just in terms of guidance as sort of housekeeping. The adjusted NPAT guidance of NZD3.30 to NZD3.70. Is that based on the old numbers pre when the actual - if you looked at the first quarter, the actual adjusted sort of NPAT number had included the cost of the earthquake and the USB so I just wanted to know whether the NZD3.30 to NZD3.70 is still like for like what we had from the first quarter. That's the first question.

Nick Olson - ***Telecom New Zealand - CFO***

Yeah, well Richard, we hadn't included the earthquake impact year to date at that point.

Richard Airey *- UBS - Analyst*

Okay. So should we say that the adjusted number doesn't include the USB and the earthquake costs?

Nick Olson *- Telecom New Zealand - CFO*

Okay.

Richard Airey *- UBS - Analyst*

The second question is just regard to looking at the mobile revenues, obviously they're still basically down year on year ex obviously the handset revenues that have come through, which is obviously a big reduction year on year. But I was just looking at the data line. There doesn't seem to be any sort of dramatic improvements over the last three or four quarters with regard to data revenue, despite the fact that XT subscriber base and particularly on the post-paid basis is pretty much doubled. So I'm just trying to understand whether the uptake in the XT base is not really delivering on the data side, or whether we're starting to see price pressure in that market that's offset or capping that data revenue potential and whether we can start to see that trend inverse going forward.

Paul Reynolds *- Telecom New Zealand - CEO*

As we've said in previous quarters Richard, we definitely see (inaudible). We take a sample of customers and did a like for like comparison of customers on CDMA versus XT and our initial figures were as high as 19%. Clearly if you go into other parts of the base the number is not as high as that, but it's still very significant and largely driven by increased (inaudible) but so many people are using all services on smart phones, voice as well as data but a lot of increased use in data. All that said, there is significant price pressure in data. We've seen some very low pricing offers in the New Zealand marketplace so some of the usage uplift has been offset by price decline. There's a limit to how far that could go and net net we are pleased that the ARPUs are lifting as you can see in the numbers. There's still a shift between categories and customers are definitely using a lot more data as we go into XT.

Richard Airey *- UBS - Analyst*

Just to ask in another way, are you comfortable with the fact that by the time we actually report the second half results that the mobile revenue trajectory is going to become more positive or become more positive or become positive?

Paul Reynolds *- Telecom New Zealand - CEO*

Well, I'm not giving a new forecast Richard but...

Richard Airey *- UBS - Analyst*

No, I wasn't asking.

Paul Reynolds *- Telecom New Zealand - CEO*

...what I would say to you is that all the underlying and core indicators are positive. Connection, ARPU, customer satisfaction, customer preference, the value preference versus a looming competitor were no higher I think for the first time in recent years. So what you saw in the last quarter, which was significantly positive is where we're going for this next reporting period. We are being very active, energetic and aggressive in the marketplace. So we think these are good signs and we'll see how we go.

Richard Airey - ***UBS - Analyst***

Then just the last question. You mentioned churn at the start of your presentation being low at 6%, which is obviously a good number within the fixed line space. How do you manage that as we go through UFB, because clearly that's an area of issue which you'd imagine would accelerate and give an opportunity for other carriers to play within that space. Is that a concern for you that obviously not only is that positive today, but could be basically a bit of a double edged sword as we move into UFB migration?

Paul Reynolds - ***Telecom New Zealand - CEO***

Richard, I missed the first sentence of your question. What were you referring to?

Richard Airey - ***UBS - Analyst***

Fixed line churn. You said fixed line churn was (inaudible) for the half, which is obviously low relative to global standards. The issue I was saying is that while that's a positive today clearly the concern is that as we go into UFB migration over a period of time, that will obviously probably escalate 90 as you deactivate and reactive customers but it gives an opportunity for your competitors to do likewise. So I mean how do you manage that process?

Paul Reynolds - ***Telecom New Zealand - CEO***

First of all I think that the good thing about the New Zealand marketplace is the free local calling regime and people are more attached to the home fixed line both for broadband and for calls then we're seeing another market and that's good news. It's good business news for us and I think we have, but it's not something that just happens. It doesn't just be there. You know we certainly found Access churn being significantly higher both in consumer and business 18 months ago than it is today.

That's the result of very focused, bundled offers, street by street offers that both Retail and Gen-i are driving into, so that's all to the good. But, you know, UFB changes the nature of the market, of course it does. We are going to see progressively over the next 20 years and 20 years is the number, progressive uptake of fiber services.

We would seek to participate in that very aggressively. I mean at the end of the day customers clearly have a strong trust in Telecom to provide fixed line services.. Currently we provide those on FTTN or sometimes exchange-based services and in the future we are going to be substituting into that fiber to the home.

Does it add a new structural dimension, does it add a significant competitive dimension. I don't think of itself it changes the market very much and in a competitive way it just changes the structure and the amount. Obviously the big issue is the investment profile and the pricing on fiber services, whether they are offered by us or indeed anybody else in the market place.

But there I think, you know, we are just pleased our strength in this marketplace, our ability to manage it has been good so far and we'll take UFB as it comes.

Richard Airey - ***UBS - Analyst***

Paul, just one final question just for Nick, just in terms of guidance for the second half in terms of expected UFB costs, clearly natural disaster costs have rolled of quarter on quarter but can we expect a similar run rate of NZD6 million for quarter on quarter running into the second half or do we expect these to drop off as we get a UFB resolution.

Nick Olson - ***Telecom New Zealand - CFO***

Okay, so UFB costs are quite uncertain at the moment and they can go several ways. If we reached a definitive deal they would go up actually because we 'd actually have to prepare for a de-merger. If it carries on like it is, we are going to carry on seeing a couple of million dollars a month in round figures and this comes to a close.

Paul Reynolds - ***Telecom New Zealand - CEO***

So it all depends how the deal goes, Richard.

Richard Airey - ***UBS - Analyst***

No, no appreciate that I am just trying to get an understanding is it, you know, where the flex is in that number.

Nick Olson - ***Telecom New Zealand - CFO***

Yeah okay.

Richard Airey - ***UBS - Analyst***

appreciate it, thanks a lot guys.

Paul Reynolds - ***Telecom New Zealand - CEO***

Thanks, Richard. Another question online?

Operator

Thank you the next question comes from Laurent Horrut of JP Morgan, Laurent, please go ahead.

Laurent Horrut - ***JP Morgan - Analyst***

Good morning, Paul and Nick, how are you?

Paul Reynolds - ***Telecom New Zealand - CEO***

How's it going, good thank you.

Laurent Horrut - ***JP Morgan - Analyst***

Okay, just first of all a question for Nick probably because I think it has got something to do with accounting. Wholesale EBITDA was down 15% you might have deferred from that amount I might have missed a comment I was a bit late on the call. That seems to be driven sort of a 58% decline on PCP, it seems to be driven by the change in the internal costing with Chorus, and also some kind of steep increase in inter-carrier costs.

So I was wondering, Nick, if you could touch on these two issues?

Nick Olson - ***Telecom New Zealand - CFO***

I must say I think we'll kick that one for touch. There are a number of moving parts in that and we could take 10 minutes to work through it. But what I'd do is just invite you to call the IR team and they'll pick it up at a forensic level.

Laurent Horrut - ***JP Morgan - Analyst***

Okay.

Paul Reynolds - ***Telecom New Zealand - CEO***

If you missed the first half, I mean the net net picture is that we are seeing strong growth in Wholesale. Wholesale lines are increasing, clearly there are a lot of moving parts on the internal trades on the back of that. But I think the macro picture when you net them all out. Because it is a...

Laurent Horrut - ***JP Morgan - Analyst***

Okay, total value for the plan thank you. Just a second question, on the UFB and I know you said there is nothing more to say, but when you look at sort of the situation in Australia it took basically 12 months to go from an HOA or it might actually even take a bit longer to from a Heads of Agreement to go to a shareholder vote.

Is that broadly the sort of time frame you would be thinking would be realistic. So in the sense that heads of agreement or whatever temporary or preliminary agreements that have to be worked out then we're looking really at a 12 month forward date from there?

Paul Reynolds - ***Telecom New Zealand - CEO***

Well Geoff asked exactly the same question, Laurent, but used different words. My answer is exactly the same. I am not going to give you a new forecast, but we gave you an indication of the complexity and potential time frames in our earlier estimate based on the notion of an agreement before Christmas.

Laurent Horrut - ***JP Morgan - Analyst***

Okay.

Paul Reynolds - ***Telecom New Zealand - CEO***

So I'll leave you to do the math and I am not going to refine that forecast.

Laurent Horrut - ***JP Morgan - Analyst***

Okay. Just to be clear, in terms of your negotiation with, I'm just looking for some clarity on sort of nature of the process rather than the actual substance. In terms of when you negotiate with UFB, is it a business to business negotiation now or, you know you kind of have to deal with the Government in that same context.

Paul Reynolds - ***Telecom New Zealand - CEO***

Sorry, negotiations...

Laurent Horrut - ***JP Morgan - Analyst***

Sorry, I should say when you are negotiating with CFH, sorry.

Paul Reynolds - ***Telecom New Zealand - CEO***

Yes, negotiations take place, CFH are the Government's agents in this, in the commercial negotiations. In terms of the policy issues, the MED are charged with the policy issues and they have been running those through some various consultation programs that I referred to earlier.

But in terms of, if you like deal terms it's with CFH.

Laurent Horrut *- JP Morgan - Analyst*

Okay, thanks guys.

Paul Reynolds *- Telecom New Zealand - CEO*

Thank you. Another question?

Operator

The next question comes from Greg Main of First New Zealand Capital, go ahead please, Greg.

Greg Main *- First New Zealand Capital - Analyst*

Hey good morning, guys.

Paul Reynolds *- Telecom New Zealand - CEO*

Morning.

Greg Main *- First New Zealand Capital - Analyst*

Yeah just a quick question actually, just on the supplier settlements. Do you expect any more or any additional supplier settlements going forward?

Paul Reynolds *- Telecom New Zealand - CEO*

Well someone asked the same question, Greg, supplier settlements happen from time to time from various suppliers and you know I am pretty sure we will get some in the future but I am not about to give a forecast season with that. So no forecast, sorry.

Greg Main *- First New Zealand Capital - Analyst*

Okay, thank you.

Operator

Mr. Reynolds, we do have one more telephone question, would you like to take it now?

Paul Reynolds *- Telecom New Zealand - CEO*

Yes.

Operator

Thank you, the next question comes from Mark McDonnell of BBY, please go ahead, Mark.

Paul Reynolds - ***Telecom New Zealand - CEO***

Okay, Mark.

Mark McDonnell - ***BBY - Analyst***

Yes, good morning. Look I am just wanting to ask you a little bit about your Labor expense. I have been looking at the supplementary information in your MD&A at page 32 and I just tried to understand the way this was working. Firstly in terms of the number of employees and then secondly the way that plays through to the actual expense line.

The advantage of this over the published accounts is it is actually showing sequential quarterly data. So for example whereas in your P&L you see a 3.9% reduction in your labor expense on the PCP on a quarterly basis, sequential quarterly basis your labor expense actually went up very slightly from NZD436 million to NZD439 million.

The reason I am asking you about this is that when you look down the page you see that the number of the FTE totals actually declined by 442 persons from 9015 to 8573. So the questions that arise from this are, firstly I assume a large part of the 442 was the AAPT Consumer business so that when we are thinking about cost-out in the future we wouldn't expect declines of the same magnitude.

But secondly I'm wondering if you could also just explain how with such a large head count reduction on a sequential half year basis the labor expenses actually went up slightly?

Paul Reynolds - ***Telecom New Zealand - CEO***

Okay, Mark, you know I think when you get down to that level there are a lot of moving parts and how things would look. I think the big picture is clearly, what is obvious in these results is our costs, our cost control and cost reduction program overall is coming in strongly.

A lot of that is driven by labor activity but there's a lot of puts and takes in the numbers and as Nick was saying, for example, next quarter we will see a bunch come in because of in sourcing from contracts. So, you know, so to spare the rest of the audience, unless anybody wants to join in, I am very happy to take that offline with the IR team and we can break back those numbers as far as we are able and give you....

Mark McDonnell - ***BBY - Analyst***

Okay, that's fine.

Paul Reynolds - ***Telecom New Zealand - CEO***

I am not dodging the issue, but...

Mark McDonnell - ***BBY - Analyst***

No, no I realize.

Paul Reynolds - ***Telecom New Zealand - CEO***

Net net big picture is good.

Mark McDonnell - ***BBY - Analyst***

Yeah, just but can you clarify it for us all what the, you know, out of the 442 head count reduction half on half, how much of that was AAPT Consumer and what it might imply about (inaudible) decline.

Paul Reynolds - ***Telecom New Zealand - CEO***

Yes. We will give you that offline, Mark.

Mark McDonnell - ***BBY - Analyst***

Okay, all right, no problem, thanks.

Paul Reynolds - ***Telecom New Zealand - CEO***

Okay.

Operator

I would like to advise there are no further questions at this time.

Paul Reynolds - ***Telecom New Zealand - CEO***

Okay. In which case, thank you very much.