Results for the six months ended 31 December 2011

24 February 2012

'Continued operating performance improvements and a successful demerger'

Adjusted results[1]	Six months ended 31 December		
	2011	2010	Change
	$m	$m	%
Adjusted operating revenue and other gains - continuing operations	2,322	2,537	(8.5)
Adjusted EBITDA - continuing operations	488	487	0.2
Adjusted EBITDA - discontinued operations	321	381	NM
Total adjusted EBITDA	809	868	(6.8)
Depreciation and amortisation expense - continuing operations	284	377	(24.7)
Adjusted earnings before tax - continuing operations	145	48	NM
Adjusted net earnings - continuing operations	99	19	NM
Total adjusted net earnings	240	158	51.9
Adjusted free cash flow	484	388	24.7
Capital expenditure	325	480	(32.3)

[1] This information is used throughout this commentary and is presented to indicate the underlying operating performance of the Group.

Key messages:

- The Chorus business was successfully demerged on 30 November 2011;
- The results for H1 FY12 include five months of internal trading with Chorus up to demerger and one month of external trading under new trading arrangements following demerger;
- Adjusted EBITDA from continuing operations increased by $1 million to $488 million;
- Adjusted net earnings from continuing operations increased by $80 million to $99 million;
- H1 FY12 capital expenditure reduced by $155 million to $325 million representing continued focus on controlled investment;
- Adjusted free cash flow improved by $96 million to $484 million;
- H1 FY12 dividend declared of 9.0 cents per share fully imputed;
- On-market share buyback of up to $300 million to take place during the 2012 calendar year; and
- Operational separation and related migration milestones revoked with regulatory reset for Telecom post demerger.

Statutory results[2]	Six months ended 31 December		
	2011	2010	Change
	$m	$m	%
Operating revenue and other gains - continuing operations	2,358	2,555	(7.7)
EBITDA - continuing operations	519	501	3.6
EBITDA - discontinued operations	1,137	369	NM
Total EBITDA	1,656	870	90.3
Depreciation and amortisation expense - continuing operations	284	377	(24.7)
Earnings before tax - continuing operations	176	62	NM
Net earnings from continuing operations	129	34	NM
Earnings from discontinued operations, net of tax	877	131	NM
Total net profit after tax	1,006	165	NM
Diluted EPS (cents)	52	9	NM

[2] Statutory results are those prepared in accordance with IFRS. For the differences between statutory and reported results, refer to the 'Non-GAAP financial measures' section.

Telecom Chief Executive, Paul Reynolds, said 'I am pleased to report that Telecom continued to deliver operating performance gains during a half year that also featured the successful demerger of its Chorus business.

The momentum built up last year has been maintained and we delivered improvements in customer satisfaction and operating efficiency, as well as real progress towards our strategic growth goals in broadband, mobile and ICT.

The demerger was probably the most complex corporate transaction in recent New Zealand history and a world's first for a telecommunications company. I am pleased it has helped deliver real value for customers and shareholders.

Following the successful demerger, Telecom is positioned for the future serving of customers and retaining number one or number two position in all core markets, through a suite of services that run on our national, mobile, data and PSTN networks.

In addition, the company can now compete on a similar footing to its competitors, due to the reduced impact of regulation in the new industry structure.

Due to the demerger timing and the associated accounting impact, year-on-year financial comparisons are complicated. However, the ongoing operational improvement in Telecom's continuing business is clear after adjusting for the significant non-cash accounting and other impacts of the demerger.

In line with the company's Vision 2013 strategy, simplification of our business has delivered both improvement to customer satisfaction and reduction in costs.

The continued focus on mobile, broadband and ICT has provided a strong platform for the future, and delivered growth in NZ broadband revenues as well as average revenue per user ('ARPU') growth in both mobile and broadband. There has also been further margin growth in IT services.

Customer satisfaction has improved in New Zealand, and the focus on simplicity and efficiency means that costs have declined faster than revenues, enabling Telecom to maintain flat EBITDA for its continuing operations.

This, along with emphasis on good control of capital expenditure, has resulted in a 25% improvement in adjusted free cash flow when compared to the first half of the previous financial year. The share buyback, announced today, will return further value to shareholders.'

Group income statement

A breakdown of the Group's reported income statement for the period ended 31 December 2011 and the prior comparative period is provided in the table below.

All information presented in this section refers to the statutory results prepared in accordance with IFRS and is before consideration of any adjusting items.

	Six months ended 31 December		
	2011	**2010**	**Change**
	$m	**$m**	**%**
Operating revenues and other gains - continuing operations			
Local service	457	486	(6.0)
Calling	394	479	(17.7)
Interconnection	53	100	(47.0)
Mobile	445	405	9.9
Data	268	291	(7.9)
Broadband and internet	238	250	(4.8)
IT services	267	274	(2.6)
Resale	93	124	(25.0)
Other operating revenue	97	114	(14.9)
Other gains	46	32	43.8
	2,358	**2,555**	**(7.7)**
Operating expenses - continuing operations			
Labour	411	421	(2.4)
Intercarrier costs	379	490	(22.7)
Other operating expenses	1,044	1,139	(8.3)
Other expenses	5	4	25.0
	1,839	**2,054**	**(10.5)**
EBITDA - continuing operations	**519**	**501**	**3.6**
Depreciation	178	259	(31.3)
Amortisation	106	118	(10.2)
Depreciation and amortisation	**284**	**377**	**(24.7)**
Earnings before interest and tax - continuing operations	**235**	**124**	**89.5**
Net finance expense	(59)	(63)	(6.3)
Share of associates' profits/(losses)	-	1	NM
Earnings before tax - continuing operations	**176**	**62**	**NM**
Income tax expense	(47)	(28)	67.9
Net earnings from continuing operations	**129**	**34**	**NM**
Earnings from discontinued operations, net of tax	877	131	NM
Net profit after tax	**1,006**	**165**	**NM**

- Operating revenue and other gains for Telecom's continuing operations of $2,358 million in H1 FY12 reduced by $197 million, or 7.7%, when compared to the prior comparative period. Mobile revenue increased in H1 FY12; however, all other revenue lines declined due to continued competition, the reduction in SMS and mobile termination rates and the effect of three months of trading relating to AAPT's Consumer division in H1 FY11. The New Zealand business saw increased revenue from broadband and internet. The significant declines in calling revenue primarily related to lower demand and pricing in the international carrier services market.
- Other gains of $46 million in H1 FY12 comprised $8 million interim insurance recoveries relating to the Canterbury earthquakes; $28 million in relation to an FX gain recycled from the foreign currency translation reserve; a $4 million gain on the sale of Gen-i's Software Solutions business; and $6 million of other gains on sale. Some of these gains are treated as adjusting items as detailed below.

- The decline in operating revenues from continuing operations was more than offset by reductions in operating expenses (excluding non-recurring other expenses), which fell by $216 million, or 10.5%, to $1,834 million in H1 FY12. For H1 FY12: reduced labour costs were a result of continued headcount reduction initiatives; lower intercarrier costs were due to the effect of lower overall pricing, including lower mobile termination rates; and reductions in other operating expenses were due to the impacts of a lower head count, ongoing focus on cost-out initiatives, the impact of a strong New Zealand dollar and H1 FY11 including three months of costs for AAPT's Consumer division. The reductions in other operating expenses were partially offset by increased mobile cost of sales arising from increased acquisition volumes and average mobile device prices, as well as CDMA migration costs in Telecom Retail.
- Other expenses of $5 million in H1 FY12 relate to further costs arising in relation to the Canterbury earthquakes. This is treated as an adjusting item as detailed below.
- The H1 FY12 combined depreciation and amortisation charges decreased by $93 million to $284 million due to the sale of AAPT's Consumer division assets in September 2010, reduced depreciation on the CDMA network which was fully depreciated during H2 FY11, and the asset impairment recognised in H2 FY11 and the flow-on effect from significant reductions in capital expenditure in the past two years.
- The net finance expense in H1 FY12 of $59 million was $4 million lower than in H1 FY11 primarily due to the debt restructuring as a result of the demerger.
- The H1 FY12 tax expense of $47 million was $19 million higher than the tax expense recognised in H1 FY11. The movement is principally due to a $33 million increase arising from higher H1 FY12 taxable earnings, partially offset by an $18 million impact in H1 FY11 as a result of a reduction in the value of certain tax credits following legislative changes, and a number of other items including the change in tax rate from the FY11 rate of 30% to the FY12 rate of 28%.
- Net earnings after tax from continuing operations of $129 million in H1 FY12 were significantly higher than the $34 million in H1 FY11, primarily due to the reductions in depreciation and amortisation charges referred to above.
- Net earnings after tax from discontinued operations of $877 million in H1 FY12 were significantly higher than the $131 million in the comparative period primarily due to the gain on disposal of the discontinued operations ('Chorus'). This gain is treated as an adjusting item as detailed below. Included in the discontinued operations result are total economic demerger transaction costs of $83 million, which comprises $36 million of financing and consent fees and $47 million of other transaction costs. There are also $10 million of financing costs that were met by Chorus. This total of $93 million compares to the $85 million to $120 million range of demerger transaction costs estimated in the Scheme Booklet.

Adjusting items and results

We use the terms 'adjusted operating revenue', 'adjusted EBITDA', 'adjusted net earnings' and 'adjusted free cash flow' to refer to such measures that reflect adjustments to our results to eliminate the effects of significant one-off gains, expenses and impairments. These are non-GAAP financial measures and are not prepared in accordance with IFRS. Management uses adjusted information to measure the underlying trends of the business and monitor performance. We believe that these adjusted financial measures give a helpful view of our results and facilitate comparisons from period to period in light of disposals and other one-off items. Our adjusted results should not be viewed in isolation or regarded as a replacement for corresponding IFRS measures, and we also note that these adjusted measures as defined or presented by us may not be comparable to similarly titled measures reported by other companies.

Chorus was demerged from Telecom and became a stand-alone company on 30 November 2011. A fair value gain of $775 million was recognised in H1 FY12 as a result of the demerger, which also crystallised certain other transactions. Results from the demerged business units are classified as a discontinued operation for H1 FY12 and therefore its results are not included in operating revenues or expenses for Telecom's continuing operations.

The revenues and expenses in this management commentary reflect the results of Telecom's continuing operations unless stated otherwise.

During H1 FY12, the adjusting items were as follows:

Adjusted for in continuing operations:

- Costs of $5 million were incurred in relation to the Canterbury earthquakes;
- Other income of $8 million in relation to insurance proceeds from the Canterbury earthquakes;
- One-off gain of $28 million in relation to the non-cash FX gain recycled from the foreign currency translation reserve; and
- $1 million of related tax effects on the above adjustments.

Adjusted for in discontinued operations:

- Transaction costs of $47 million incurred in effecting the demerger;
- Gain of $775 million arising from the demerger of the Chorus business. The gain on demerger represents the difference between the fair value and the carrying value of the net assets transferred to Chorus;
- One-off net gain of $88 million in relation to entering into finance leases and jointly controlled asset arrangements with Chorus on demerger;
- Debt restructuring costs of $110 million, including $74 million of accounting costs of closing out hedge arrangements and $36 million of transaction-related financing and consent fees; and
- $30 million of related tax effects on the above adjustments.

During H1 FY11, the adjusting items were as follows:

- The Consumer division of AAPT's operations was sold to iiNet for A$60 million. This sale resulted in a gain of NZ$18 million;
- Costs of $4 million were recognised in relation to the Canterbury earthquakes, comprised of incremental operational costs incurred, customer credits and asset impairments;
- Costs of $12 million were incurred in relation to Telecom's UFB proposal; and
- $5 million of related tax effects on the above adjustments.

A reconciliation of reported total net earnings to adjusted total net earnings, both including earnings from discontinued operations, is shown in the table below.

	Six months ended 31 December		
	2011	2010	Change
	$m	$m	%
Reported net earnings	**1,006**	**165**	**NM**
Adjusted for in continuing operations:			
Gain on sale of AAPT consumer division	-	(18)	NM
Natural disaster costs	5	4	25.0
Earthquake insurance claim proceeds	(8)	-	NM
Recycled FX gain from FCTR	(28)	-	NM
Related tax effects	1	(1)	NM
Adjusted for in discontinued operations:			
Demerger-related costs	47	-	NM
UFB costs	-	12	NM
Gain on distribution of Chorus shares	(775)	-	NM
Net gain on asset arrangements between Chorus and Telecom	(88)	-	NM
Debt restructuring costs	110	-	NM
Related tax effects	(30)	(4)	NM
Adjusted net earnings	**240**	**158**	**51.9**

An analysis of Telecom's adjusted results is set out below:

	Six months ended 31 December		
	2011	2010	Change
	NZ$m	NZ$m	%
Adjusted operating revenue and other gains			
Wholesale & International	387	527	(26.6)
Retail	962	1,012	(4.9)
Gen-i	683	714	(4.3)
AAPT	370	477	(22.4)
T&SS	279	305	(8.5)
Corporate	107	91	17.6
Revenues from Chorus discontinued operations	21	29	(27.6)
Eliminations	(487)	(618)	(21.2)
Adjusted operating revenue and other gains	**2,322**	**2,537**	**(8.5)**
Adjusted EBITDA			
Wholesale & International	79	75	5.3
Retail	233	240	(2.9)
Gen-i	123	105	17.1
AAPT	40	46	(13.0)
T&SS	1	-	NM
Corporate	12	21	(42.9)
Discontinued operations	321	381	(15.7)
Adjusted EBITDA	**809**	**868**	**(6.8)**
Adjusted net earnings	240	158	51.9
Adjusted free cash flow	484	388	24.7

- Adjusted operating revenue and other gains declined by 8.5% to $2,322 million in H1 FY12 when compared to H1 FY11. The explanation of the decline is as described above; however, adjusted revenue excludes the $28 million foreign exchange gain and $8 million insurance recoveries.

- Adjusted EBITDA decreased by 6.8% to $809 million in H1 FY12 due largely to the reduced earnings from Telecom's discontinued operations, which contributed EBITDA for five months in H1 FY12 compared to six months in H1 FY11. The H1 FY12 result also included an adverse EBITDA impact arising from settlement of the SLU/SLES litigation matter made prior to demerger.
- Adjusted net earnings of $240 million in H1 FY12 improved significantly when compared to the $158 million in H1 FY11 primarily due to the reductions across all operating expense lines, which offset revenue declines, and reduced depreciation and amortisation expenses.
- Telecom's adjusted free cash flow (defined as total adjusted EBITDA less capital expenditure) in H1 FY12 of $484 million increased by $96 million, or 24.7%, when compared to H1 FY11. The H1 FY12 increase was attributable to a reduction in capital expenditure of $155 million over the comparative period, partially offset by a reduction in total adjusted EBITDA, including discontinued operations, of $59 million.

Review of operations

Telecom's business units currently comprise Wholesale & International, Retail, Gen-i, and AAPT and they are supported by a technology and shared services unit ('T&SS'). In addition to these operating segments, the results of which are reported to Telecom's CEO, there is also a central product group and a corporate centre.

The results by business unit have historically incorporated internal trading as required by the Undertakings. These trades predominantly related to regulated services, as provided by Chorus and Wholesale. Field services that supported the provision of regulated services, as stipulated in the Undertakings, were also sold internally by Chorus. The Chorus and regulated Wholesale trades are no longer internal charges within Telecom post-demerger and, instead, have now become external trading arrangements.

Telecom's results are reported on a fully allocated basis, where 'Full Cost Apportionment' ('FCA') aims to match costs with revenues and has resulted in a portion of internal trades that allocate substantially all the costs from T&SS and certain Corporate costs to customer facing business units, as well as a number of external interconnection revenues and costs currently recognised in Wholesale being allocated to other business units. Certain FCA costs historically allocated to Chorus have not been included within the discontinued operations results where these costs will not be replaced by similar charges under new trading arrangements with Telecom. These costs have instead been absorbed within the Corporate result in continuing operations.

In addition to the operational separation trades and FCA, Wholesale & International derive internal revenue from the provision and supply of international data circuits, the supply of international internet services, and the termination of international voice traffic offshore.

All internal transactions are eliminated on consolidation. However, the comparative results have been re-presented as if the Chorus business discontinued during the current year had been discontinued from the start of the comparative period. Certain comparative numbers have therefore been restated to reflect changes to Telecom's internal trading arrangements and certain other comparative information has also been reclassified to conform with the current period's presentation. There is no change to the overall Group reported result.

The business unit results exclude significant one-off gains, expenses and impairments. These items are excluded from the business unit results to enable an analysis of the underlying earnings when the financial results are presented to Telecom's CEO.

During FY11, Telecom launched a strategic programme called Vision 2013, being a call to action for the business in recognising a tougher operating environment and a need for increased initiatives in operating excellence, cost reduction and capital intensity.

In April 2011, Telecom announced the establishment of a central product group. Using Telecom's strategy, the central product group assesses product/service portfolios, including whether to exit non-core services, outsourcing activities to strategic partners better able to compete (eg, non-telecommunication retailers in price-sensitive segments) and acquiring capabilities to participate in new markets, through strategic alliances or partnerships.

Business unit and corporate commentaries

All information presented in the following individual business unit and corporate commentaries refers to adjusted results, incorporating the adjusting items referred to above.

Wholesale & International

Wholesale provides business data, voice and interconnect products and services to telecommunications service providers in New Zealand. These products and services are provided either as inputs that allow Wholesale's customers to build and deliver their own tailored services or on a resale basis allowing customers to resell the equivalent of retail based services to their own customers. Wholesale also manages Telecom's internet carriage and transit to and from New Zealand and Australia, over the Southern Cross and SMW3 cables, with a range of peering networks in the USA and Australia, as well as providing data services in North America and Australia.

International provides international voice services to other Telecom business units and to over 100 global customers, serviced through points of presence in North America, Europe and Asia.

	Six months ended 31 December		
	2011	**2010**	**Change**
	$m	**$m**	**%**
Operating revenues			
Local service	117	107	9.3
Calling	103	136	(24.3)
Interconnection	35	80	(56.3)
Mobile	2	4	(50.0)
Data	49	42	16.7
Broadband and internet	-	1	NM
Other operating revenue	10	13	(23.1)
Internal revenue	65	144	(54.9)
Other gains	6	-	NM
	387	**527**	**(26.6)**
Operating expenses			
Labour	12	20	(40.0)
Intercarrier costs	140	226	(38.1)
Other operating expenses	8	21	(61.9)
Internal expenses	148	185	(20.0)
	308	**452**	**(31.9)**
EBITDA	**79**	**75**	**5.3**
FTE - Permanent	171	340	(49.7)
FTE - Contractors	2	6	(66.7)
FTE - Total	**173**	**346**	**(50.0)**

Operating revenues

Wholesale & International's revenue decreased by 26.6% to $387 million in H1 FY12 when compared to the prior comparative period.

Local service revenues increased by 9.3% to $117 million in H1 FY12, primarily reflecting growth in the number of fixed access lines, with connections increasing by 3.7% from 402,000 lines at 31 December 2010 to 417,000 lines at 31 December 2011, combined with a CPI price increase from October 2010.

Calling revenues decreased by 24.3% to $103 million in H1 FY12 as a result of the competition in the international market causing a fall in the average price per minute, as well as exiting low margin customer arrangements.

Interconnection revenues have decreased by $45 million, or 56.3%, to $35 million in H1 FY12 primarily due to decreases in SMS rates and mobile termination rates.

Mobile revenues decreased by $2 million to $2 million in H1 FY12, predominantly due to a migration of customers from a CDMA network Mobile Virtual Network Operator (‘MVNO’) to a competitor at the end of FY11.

Data revenues increased by $7 million to $49 million in H1 FY12 driven by growth with existing customers.

Internal revenues decreased by $79 million to $65 million in H1 FY12 due primarily to the reduction in SMS and mobile termination rates, which reduced termination cost recharges to other Telecom business units. New internal trading arrangements with other business units, combined with calling volume declines from the Telecom channels, also contributed to the decline.

Other gains of $6 million in H1 FY12 arose on the sale of IRU capacity.

Operating expenses

Wholesale & International’s operating expenses decreased by $144 million to $308 million in H1 FY12 when compared to the prior comparative period.

Labour costs decreased by $8 million, or 40.0%, to $12 million in H1 FY12, reflecting lower FTE levels and cost-saving initiatives. From 1 December 2011, no FTEs remain in Wholesale, with these employees either transferring to Chorus or being integrated into Corporate.

Intercarrier costs decreased by $86 million, or 38.1%, to $140 million in H1 FY12, primarily due to lower costs per minute in the carrier services market, exiting low margin customer arrangements, decreases in SMS and mobile termination rates and a decrease in interconnection outbound SMS volumes.

Other operating expenses decreased by 61.9% to $8 million due to the effect of cost-out initiatives in the carrier services business and a favourable foreign exchange impact arising from the strength of the NZ dollar.

Internal expenses decreased by $37 million to $148 million in H1 FY12 due to lower internal costs as a result of a lower allocation of interconnect revenue following the decrease in SMS and mobile termination rates.

Wholesale and International’s EBITDA increased by $4 million, or 5.3%, to $79 million in H1 FY12 when compared to H1 FY11 as growth in data and local service revenues and a decrease in expenses more than offset other revenue declines.

Retail

Retail provides mass market products, services and support to consumer and commercial customers. As a full service provider, Retail provides fixed-line calling and access products, broadband, dial-up and online offerings, mobile voice, SMS / text, content and data services.

	Six months ended 31 December		
	2011	2010	Change
	$m	$m	%
Operating revenues			
Local service	296	320	(7.5)
Calling	134	155	(13.5)
Mobile	328	296	10.8
Data	9	10	(10.0)
Broadband and internet	158	150	5.3
IT services	4	6	(33.3)
Other operating revenue	11	14	(21.4)
Internal revenue	22	61	(63.9)
	962	**1,012**	**(4.9)**
Operating expenses			
Labour	66	75	(12.0)
Intercarrier costs	26	-	NM
Other operating expenses	218	185	17.8
Internal expenses	419	512	(18.2)
	729	**772**	**(5.6)**
EBITDA	**233**	**240**	**(2.9)**
FTE - Permanent	1,740	2,004	(13.2)
FTE - Contractors	123	101	21.8
FTE - Total	**1,863**	**2,105**	**(11.5)**

Operating revenues

Retail's operating revenues in H1 FY12 of $962 million decreased by $50 million, or 4.9%, when compared to H1 FY11. Local service, calling, data, IT services and other revenue declines in H1 FY12 of $51 million were partially offset by $40 million of growth in mobile and broadband and internet revenues.

Local service and calling revenues declined in H1 FY12 by a combined $45 million, or 9.5%, to $430 million when compared to H1 FY11 due to continued customer churn and calling price reductions.

Retail access lines decreased by 6.9% from 1.099 million at 31 December 2010 to 1.023 million at 31 December 2011. Retail continues to focus on product bundling, to provide greater value to customers with multiple product holdings, driving overall ARPU growth and retaining the existing base.

Calling revenue decreased 13.5% in H1 FY12 primarily due to the lower access line base, but also due to the re-pricing of key calling categories, including fixed to mobile price reductions following regulatory mobile termination rate adjustments. International and fixed to mobile price reductions in H1 FY12 have partly mitigated increasing calling churn.

Broadband and internet revenues increased by $8 million, or 5.3%, to $158 million in H1 FY12 when compared to H1 FY11. Despite an increase in price-based competition in the market, broadband connections of 598,000 increased by 18,000, or 3.1%, when compared to H1 FY11.

Mobile revenues (including Retail and Gen-i) increased by $47 million, or 12.0%, to $438 million in H1 FY12 when compared to H1 FY11, due to increased device revenues and a change in accounting for mobile subsidies.

Telecom's mobile customer base (including Telecom Retail, Gen-i, and Telecom Wholesale connections) decreased by 3.1% to 2.031 million customers at 31 December 2011 from 2.097 million customers at 30 June 2011. This decline has been affected by an increased volume of CDMA customers churning to other networks as the CDMA network shutdown in July 2012 approaches. Consequently, the prepaid base has decreased by 92,000 since 30 June 2011, although prepaid ARPU increased 6.9% to $10.29 when compared to H2 FY11, highlighting that the customer losses are predominantly low-value.

Retail's continued focus on smartphone penetration and acquisition of high-value customers, together with further migration of customers from prepaid to postpaid plans, has delivered significant growth in the postpaid base during H1 FY12, with a net increase of 27,000 connections since 30 June 2011. The launch of the iPhone 4S during the Christmas campaign was a significant driver of the strong postpaid growth in H1 FY12.

At 31 December 2011, 1.392 million customers were on the XT network, with XT connections up 209,000, or 17.7%, from 30 June 2011. 639,000 customers, or 31.5% of the mobile base, remain on the CDMA network at 31 December 2011 compared to 43.6% of the base as at 30 June 2011.

Mobile ARPU increased by 8.6% to $29.18 in H1 FY12 when compared to $26.87 in H1 FY11. While mobile voice revenues declined by $6 million, or 2.9%, in H1 FY12 compared to H1 FY11, this was more than offset by $11 million, or 8.1%, growth in data revenues (including text) over the same period. The strong data revenue growth was driven by the increased number of higher value customers acquired.

Fixed data revenues in H1 FY12 decreased by $1 million, or 10.0%, to $9 million when compared to H1 FY11, reflecting a reduction in ISDN usage resulting from lower customer numbers and calling minutes.

Internal revenue decreased by $39 million, or 63.9%, to $22 million in H1 FY12 when compared to H1 FY11 due to reduced interconnection revenues following a regulatory reduction in mobile termination rates.

Operating expenses

Continued focus on cost efficiency has continued to drive labour expenses to the lowest level in recent periods of $66 million for H1 FY12, being $9 million, or 12.0%, lower than H1 FY11. Restructuring activities have reduced permanent headcount by 13.2% at 31 December 2011 when compared to 31 December 2010.

Other operating expenses increased by $33 million, or 17.8%, to $218 million in H1 FY12 when compared with H1 FY11. This was largely driven by increased mobile cost of sales arising from increased volumes, higher average value of mobile device sales and costs in relation to CDMA migration.

Intercarrier costs of $26 million were incurred in H1 FY12 representing the first month's new baseband charges from Chorus. Prior to demerger, these telephone access costs were allocated to Retail in internal expenses.

Internal expenses have decreased significantly to $419 million in H1 FY12, an 18.2% reduction when compared to H1 FY11. This is largely as a result of a decline in interconnection charges, following reduced mobile termination rates, the new trading arrangements implemented following demerger and the lower access base.

Gen-i

Gen-i's goal is to become Australasia's most preferred ICT hosted services and integrated ICT solutions provider, delivering brilliant outcomes for its clients.

	Six months ended 31 December		
	2011	**2010**	**Change**
	$m	**$m**	**%**
Operating revenues			
Local service	44	50	(12.0)
Calling	68	75	(9.3)
Mobile	110	95	15.8
Data	140	168	(16.7)
Broadband and internet	8	11	(27.3)
IT services	263	268	(1.9)
Resale	1	2	(50.0)
Other operating revenue	6	7	(14.3)
Internal revenue	39	38	2.6
Other gains	4	-	NM
	683	**714**	**(4.3)**
Operating expenses			
Labour	156	171	(8.8)
Intercarrier costs	5	-	NM
Other operating expenses	214	230	(7.0)
Internal expenses	185	208	(11.1)
	560	**609**	**(8.0)**
EBITDA	**123**	**105**	**17.1**
FTE - Permanent	2,328	2,658	(12.4)
FTE - Contractors	144	319	(54.9)
FTE - Total	**2,472**	**2,977**	**(17.0)**

The results for Gen-i are presented separately under the headings Gen-i telecommunications solutions and Gen-i IT solutions. Sales and support costs are included within the telecommunications results. Gen-i's IT solutions business has lower margins and lower capital expenditure requirements than the telecommunications business activities. Many of Gen-i's clients require an ICT package combining both telecommunications and IT solutions.

Gen-i telecommunications solutions

	Six months ended 31 December		
	2011	2010	Change
	$m	$m	%
Operating revenues			
Local service	44	50	(12.0)
Calling	68	75	(9.3)
Mobile	110	95	15.8
Data	139	168	(17.3)
Broadband and internet	8	11	(27.3)
IT services	26	31	(16.1)
Resale	1	2	(50.0)
Other operating revenue	5	6	(16.7)
Internal revenue	20	28	(28.6)
	421	**466**	**(9.7)**
Operating expenses			
Labour	72	91	(20.9)
Intercarrier costs	5	-	NM
Other operating expenses	66	83	(20.5)
Internal expenses	174	202	(13.9)
	317	**376**	**(15.7)**
EBITDA	**104**	**90**	**15.6**
FTE - Permanent	880	1,102	(20.1)
FTE - Contractors	25	78	(67.9)
FTE - Total	**905**	**1,180**	**(23.3)**

Operating revenues – Telecommunications solutions

Traditional local service and calling revenues continue to decline in H1 FY12.

Local service revenues in H1 FY12 declined by $6 million to $44 million as customers consolidated lines and moved to IP-based services.

Calling revenues declined by $7 million to $68 million when compared to the prior comparative period reflecting the combined effect of lower volumes and prices.

Mobile revenues of $110 million in H1 FY12 increased by $15 million reflecting continued strong growth in connections and increased data revenues from growth in smartphone uptake.

Data revenue decreased by $29 million to $139 million in H1 FY12 when compared with the prior comparative period primarily due to the exit of a significant financial services client in Australia, as well as decline in legacy copper-based products and increased competition.

IT services revenue decreased by $5 million to $26 million in H1 FY12 primarily due to the exit of the aforementioned financial services client in Australia and a reclassification of revenue to data.

Internal revenue has decreased by $8 million to $20 million in H1 FY12 due to lower revenue from interconnection.

Operating expenses – Telecommunications solutions

Labour costs decreased by $19 million, or 20.9%, to $72 million in H1 FY12 when compared with the prior comparative period due to lower FTE levels. In addition, the reduction reflects centralisation of, and cost savings in, support functions that are now charged to Gen-i through internal cost allocation.

Other operating expenses decreased by $17 million to $66 million in H1 FY12, reflecting lower cost of sales, partially due to the exit of the aforementioned financial services client in Australia, and reduced expenses relating to the lower FTE numbers.

Internal expenses declined by $28 million to $174 million in H1 FY12 primarily due to a reduction of business in Gen-i Australia as well as a movement of costs from internal to external intercarrier costs arising from the new post-demerger trading arrangements.

Gen-i IT solutions

	Six months ended 31 December		
	2011	**2010**	**Change**
	$m	**$m**	**%**
Operating revenues			
Data	1	-	NM
IT services	237	237	-
Other operating revenue	1	1	-
Internal revenue	19	10	90.0
Other gains	4	-	NM
	262	**248**	**5.6**
Operating expenses			
Labour	84	80	5.0
Other operating expenses	148	147	0.7
Internal expenses	11	6	83.3
	243	**233**	**4.3**
EBITDA	**19**	**15**	**26.7**
FTE - Permanent	1,448	1,556	(6.9)
FTE - Contractors	119	241	(50.6)
FTE - Total	**1,567**	**1,797**	**(12.8)**

Operating revenues – IT solutions

IT solutions revenue increased by $14 million or 5.6%, to $262 million in H1 FY12, when compared to the prior comparative period.

Internal revenue increased by $9 million to $19 million in H1 FY12 due to bringing in-house end user support and higher customer-related costs being on-charged to other business units.

Other gains of $4 million arose on the sale of the Software Solutions business.

Operating expenses – IT solutions

Total operating expenses increased by $10 million to $243 million in H1 FY12, primarily driven by increased labour costs, matching trends in revenue and internal expenses.

Labour costs increased by $4 million, or 5.0%, when compared to the prior comparative period. This was primarily due to lower net project labour cost recoveries to other parts of Telecom, together with reduced capitalisation of costs and lower non-IT related utilisation. These increases were greater than the cost savings arising from FTE reductions.

Internal expenses increased by $5 million to $11 million due to reclassification of costs in Australia and an increase in internally charged lease costs in New Zealand.

AAPT

AAPT is an Australian telecommunications provider that owns and operates its own national voice and data network. This includes nation-wide diverse coverage of 11,000km of interstate fibre, its own data centres in major capital cities, fibre access to 1,300 buildings and Midband Ethernet in over 185 exchanges. AAPT has access to DSL coverage in over 380 exchanges focused on the major Australian cities and large metropolitan areas.

AAPT has two customer segments, Wholesale and Business Solutions. Wholesale focuses on leveraging AAPT's network reach particularly within the 'on-net' data and internet sales to the carrier, partner and reseller channels. Business Solutions addresses the corporate, medium and small enterprise segments and is focused on selling 'on-net' data and internet. The Consumer division was sold to iiNet on 30 September 2010 for A$60 million. The gain on the sale of the Consumer division has been excluded from these adjusted results.

To eliminate the impact of foreign exchange rate movements, AAPT's results are presented in Australian dollars ('A$').

	Six months ended 31 December		
	2011	**2010**	**Change**
	A$m	**A$m**	**%**
Adjusted operating revenues			
Local service	-	8	NM
Calling	70	88	(20.5)
Interconnection	14	15	(6.7)
Mobile	4	8	(50.0)
Data	55	56	(1.8)
Broadband and internet	56	70	(20.0)
Resale	71	95	(25.3)
Other operating revenue	2	3	(33.3)
Internal revenue	17	32	(46.9)
	289	**375**	**(22.9)**
Operating expenses			
Labour	51	59	(13.6)
Intercarrier costs	162	207	(21.7)
Other operating expenses	29	48	(39.6)
Internal expenses	16	23	(30.4)
	258	**337**	**(23.4)**
Adjusted EBITDA	**31**	**38**	**(18.4)**
FTE - Permanent	768	882	(12.9)
FTE - Contractors	14	34	(58.8)
FTE - Total	**782**	**916**	**(14.6)**

Adjusted operating revenues

Adjusted operating revenues decreased by A$86 million to A$289 million in H1 FY12 as revenue declined in all categories. A$38 million of the revenue decline is the net reduction in revenue due to the sale of the Consumer division, which has affected calling, local service, broadband and internet and resale revenues. Business Solutions and Wholesale also experienced a A$51 million decrease in revenue when compared to H1 FY11 primarily due to customer churn and the continued rationalisation of low-margin Wholesale customers, pricing pressure and market consolidation prior to NBN going live that has resulted in some AAPT customers shifting business to other providers.

Operating expenses

Labour costs decreased in H1 FY12 by A$8 million to A$51 million when compared to the prior comparative period, primarily due to the 14.6% lower headcount which was driven by restructuring to align to the new business structure.

Intercarrier costs reduced by A$45 million to A$162 million in H1 FY12 when compared to the prior comparative period in line with reduced revenue, reflecting the focus on higher margin data and internet sales, partially offset by less favourable terms agreed with Telstra in FY12.

Other operating expenses reduced by A$19 million to A$29 million in H1 FY12 when compared to the prior comparative period. The reduction was driven by cost savings through the sale of the Consumer division, exiting contracts, billing system rationalisation and the exit of CBD office space.

Technology & Shared Services

T&SS maintains and develops all of Telecom's New Zealand shared IT and network operations. The T&SS team ensures Telecom's IT, infrastructure and architecture is aligned with the wider Group's business objectives. In addition to the core technology teams, the shared services division of T&SS supports Telecom in areas such as supply chain, provisioning, billing, engineering, operations and information management.

Under FCA, T&SS allocates costs to each of the market facing business units, based on their use of T&SS resources, or where applicable, the volumes they drive through T&SS. The charge to other business units is presented as internal revenue in T&SS and internal expenses in the other business units.

	Six months ended 31 December		
	2011	**2010**	**Change**
	$m	**$m**	**%**
Operating revenues and other gains			
Other operating revenue	14	4	NM
Internal revenue	265	287	(7.7)
Other gains	-	14	NM
	279	**305**	**(8.5)**
Adjusted operating expenses			
Labour	62	53	17.0
Other operating expenses	123	150	(18.0)
Internal expenses	93	102	(8.8)
	278	**305**	**(8.9)**
Adjusted EBITDA	**1**	**-**	**NM**
FTE - Permanent	1,766	1,430	23.5
FTE - Contractors	117	225	(48.0)
FTE - Total	**1,883**	**1,655**	**13.8**

Operating revenues and other gains

Other operating revenue largely consists of three components being cost recovery for use of T&SS's assets by external parties, provision of services by T&SS to external parties and, in some instances, credits received from third party suppliers. Other operating revenue increased by $10 million in H1 FY12 due to a combination of new trading arrangements and rebate income.

Other gains of $14 million in H1 FY11 represented settlements reached with suppliers.

Through FCA, T&SS recovers its net costs from the other business units. Internal revenue therefore mirrors and fluctuates in line with total operating expenses and other revenues.

Adjusted operating expenses

Adjusted labour costs increased by $9 million in H1 FY12 when compared to H1 FY11. The increase was predominantly related to the in-sourcing of functions, and resulting headcount, from Hewlett Packard ('HP'). These labour costs were previously recognised in other operating expenses.

Other operating expenses decreased by $27 million in H1 FY12 when compared to the prior comparative period. The decrease relates to the savings from the HP in-sourcing, as well as ongoing focus on cost out programmes.

Internal expenses decreased by $9 million in H1 FY12 when compared to the prior comparative period. This was driven by a reduction in FCA charges as a result of demerger, partially offset by new internal costs due to the in-sourcing noted above with some external costs previously charged by HP now being charged from Gen-i.

Corporate

Telecom is supported by a corporate centre, which provides leadership, finance, communications, strategy, human resources and legal functions for the Group. A central product group was established as part of the Vision 2013 strategy and its costs are included in the corporate centre. Revenue includes dividends received from Southern Cross and other revenue not directly associated with a business unit. Certain corporate revenues and costs are allocated under FCA to other business units.

	Six months ended 31 December		
	2011	2010	Change
	$m	$m	%
Operating revenues			
Other operating revenue	33	43	(23.3)
Internal revenue	74	48	54.2
	107	**91**	**17.6**
Adjusted operating expenses			
Labour	51	27	88.9
Other operating expenses	26	27	(3.7)
Internal expenses	18	16	12.5
	95	**70**	**35.7**
Adjusted EBITDA	**12**	**21**	**(42.9)**
FTE - Permanent	643	241	NM
FTE - Contractors	46	18	NM
FTE - Total	**689**	**259**	**NM**

Operating revenues

Other operating revenue decreased by $10 million in H1 FY12 when compared to the prior comparative period. The decrease in H1 FY12 was primarily due to $26 million of Southern Cross dividend income in H1 FY12 compared to $39 million in H1 FY11. Southern Cross dividends vary in amount and timing and are denominated in USD.

Internal revenue of $74 million was $26 million higher in H1 FY12 than the prior comparative period, primarily due to increased recoveries under FCA.

Adjusted operating expenses

Adjusted labour costs of $51 million have increased by $24 million in H1 FY12 when compared with the prior comparative period predominantly due to an increase in the number of FTEs arising from the centralisation of certain support functions from business units into corporate and the establishment of the central product group.

Adjusted other operating expenses decreased by $1 million to $26 million for H1 FY12 as cost savings more than offset increased costs transferred to corporate as part of centralisation.

Discontinued operations

The Chorus business was demerged on 30 November 2011 and is reported as a discontinued operation. Chorus earnings for the period up to the demerger date (30 November 2011) are included in the H1 FY12 discontinued results below. The results of the discontinued operations, comprising Chorus, regulated Wholesale and other costs related to the demerged business, are presented below and represent the reported earnings prior to adjusting items (detailed earlier in this document).

	Five months ended 30 November	Six months ended 31 December
	2011	**2010**
	$m	**$m**
Operating revenues		
Local service	13	13
Data	9	8
Broadband and internet	44	40
Other operating revenue	13	14
Internal revenues from Telecom continuing operations	417	465
	496	540
Operating expenses		
Labour	17	18
Other operating expenses	137	112
Internal costs from Telecom continuing operations	21	29
EBITDA	**321**	**381**
Depreciation	84	130
Amortisation	21	23
Net finance costs	20	26
Earnings before income tax	**196**	**202**
Income tax expense on earnings	(55)	(63)
Earnings after tax before one-off items	**141**	**139**
Gain on distribution of Chorus shares	775	-
Net gain on asset arrangements between Chorus and Telecom	88	-
Debt restructuring costs	(110)	-
Other expenses	(47)	(12)
Tax benefit on demerger related items	30	4
Net earnings for the period	**877**	**131**

The trading results in the table above represent those of the discontinued operations for the five months ended 30 November 2011 for H1 FY12 compared to six months ended 31 December 2010 in H1 FY11.

Broadband and internet revenues increased in line with wholesale connection growth, with other revenues tracking in line with previous trends and broadly in line with the prior comparative period.

Other operating expenses in H1 FY12 included an adverse $20 million EBITDA impact arising from settlement of the SLU/SLES litigation matter made prior to demerger.

Depreciation and amortisation in H1 FY12 was incurred up until 26 October 2011, being the date of the shareholder vote, as required by NZ IFRS 5: Assets Held for Sale and Discontinued Operations.

Net finance costs represent the underlying interest cost calculated on the proportion of GBP debt novated to Chorus.

All items below the 'earnings after tax before one-off items' line are adjusting items relating to demerger and considered in more detail above.

Group cash flow

The cash flow information presented below includes cash flows arising from continuing and discontinued operations.

	Six months ended 31 December		
	2011	2010	Change
	$m	$m	%
Cash flows from operating activities	504	533	(5.4)
Cash flows from investing activities	(395)	(420)	(6.0)
Cash flows from financing activities	(114)	(113)	0.9
Foreign exchange movement	1	(7)	NM
Net movement in cash	**(4)**	**(7)**	**(42.9)**

Detailed disclosure of the above line items is included in Telecom's condensed financial statements which have been released with this management commentary.

Cash flows from operating activities

Net cash from operating activities decreased in H1 FY12 by $29 million to $504 million when compared to H1 FY11. This was primarily due to a $101 million reduction in cash received from customers and a $13 million decrease in SX dividend received, which were partially offset by a $110 million reduction in payments to suppliers and employees. The decline in cash received from customers follows the overall declining revenue trend and was also affected by other working capital requirements, while supplier and employee payments have reduced due to cost saving initiatives. Tax payments of $84 million in H1 FY12, largely relating to provisional tax payments and supplementary dividends paid to non residents, increased by $10 million when compared to the prior comparative period.

Cash flows from investing activities

The net cash outflow on investing activities of $395 million in H1 FY12 was $25 million lower than the $420 million outflow in H1 FY11 largely due to a $192 million reduction in capital expenditure payments in H1 FY12, due to management's capital interventions, combined with $5 million of proceeds from the sale of the Software Solutions business. This was partially offset by the one-off $176 million of proceeds in H1 FY11 from the sale of the AAPT Consumer division, Telecom's stakes in iiNet and Macquarie Telecom and the proceeds from the Yahoo!Xtra sale.

Cash flows from financing activities

Telecom's outflows from financing activities largely reflect borrowing activities and dividend payments to shareholders. The net cash outflow for financing activities in H1 FY12 was $114 million, compared to a cash outflow of $113 million in H1 FY11. H1 FY12 comprises $183 million of dividend payments compared to $177 million in H1 FY11. During H1 FY12 Telecom repaid a net $1,279 million of long-term debt and derivatives compared to $19 million in H1 FY11. The repayment was offset by a net receipt on short-term debt of $1,442 million, of which $1,106 million was included in the Chorus net assets demerged. One-off debt restructuring costs of $211 million were paid in H1 FY12. Telecom also received $110 million of released collateral funds compared to payments of $23 million in H1 FY11 and net $7 million receipts from finance lease arrangements.

Capital expenditure

The capital expenditure information presented below incorporates both continuing and discontinued operations expenditure.

	Six months ended 31 December		
	2011	**2010**	**Change**
	$m	**$m**	**%**
Transformation and regulation			
WCDMA mobile network	42	63	
FTTN	40	68	
FNT	-	7	
Retail NGT	23	40	
Separation	12	57	
UFB	43	-	
RBI	11	-	
Other regulatory	1	2	
Total transformation and regulation	172	237	(27.4)
Business sustaining			
IT systems	25	29	
Gen-i	20	37	
AAPT	18	39	
Southern Cross capacity	1	-	
Network maintenance and growth	55	73	
New products and services	11	29	
Other business sustaining	23	36	
Total business sustaining	153	243	(37.0)
Total	**325**	**480**	**(32.3)**

Total capital expenditure for H1 FY12 of $325 million was $155 million, or 32.3%, less than H1 FY11, with decreased expenditure in all business sustaining initiatives and also an overall decrease in Transformation and Regulation expenditure.

The reduction in capital expenditure partially relates to the demerger of Chorus on 30 November 2011. H1 FY12 includes five months of Chorus-related spend, compared to six months in H1 FY11.

The H1 FY12 total capital expenditure of $325 million includes approximately $150 million of Chorus-related spend.

Transformation and Regulation

Spend on the XT network decreased to $42 million in H1 FY12 from $63 million in H1 FY11, due to decreased spending on radio network controller deployment with the high capital expenditure in FY11 relating to increased network resilience. Significantly high levels of mobile network spending in the past have now led to the lower spend in the current period.

The Chorus related FTTN investment continued as planned, with the programme winding down in FY12. As a result, spend in H1 FY12 of $40 million was $28 million lower than in H1 FY11.

FNT had no capital expenditure in H1 FY12 as the programme was completed in FY11.

Retail NGT investment of $23 million was $17 million less in H1 FY12 when compared to H1 FY11, as the broadband aggregation was completed in H1 FY11 and is now in a migration phase.

Capital expenditure relating to operational separation decreased to $12 million in H1 FY12, compared with $57 million in H1 FY11, due to certain operational separation commitments being met, or developed, during FY11.

There were two new capital expenditure initiatives in H1 FY12. UFB-related capital expenditure was $43 million and the spend on RBI was $11 million. RBI related solely to Chorus, while a significant proportion of the UFB spend was Chorus-related.

Business Sustaining

Expenditure on IT systems of $25 million was $4 million lower in H1 FY12 than H1 FY11 due to fewer one-off licence payments to vendors and a general slowing in the level of activity.

Gen-i spend in H1 FY12 of $20 million was $17 million lower than H1 FY11, primarily due to H1 FY11 spend including a one-off capital investment for client-driven customer premises equipment and delays in starting major initiatives in H1 FY12.

AAPT spend of $18 million in H1 FY12 was $21 million lower than H1 FY11 due to deferral of certain infrastructure projects.

Network maintenance and growth spend of $55 million was $18 million lower than in H1 FY11. The lower spend reflects the end of transport investment that primarily supports FTTN and better use of core network capacity meaning further significant investment is not required until H2 FY12 and possibly until FY13.

New products and services spend of $11 million was lower than the $29 million in H1 FY11 due to the current strategic focus on sustaining expenditure.

Dividend policy and long-term capital management

Long-term capital management

Telecom's principal sources of liquidity are operating cash flows and external borrowing from established debt programmes and bank facilities.

On 30 November 2011 Telecom demerged Chorus into a separate listed entity. Post the demerger the Telecom board continues to be committed to Telecom maintaining an 'A band' credit rating and its capital management policies are designed to ensure this objective is met. To that end, Telecom intends to manage its debt levels to ensure that the ratio of net interest bearing debt (inclusive of associated derivatives) to EBITDA does not materially exceed 1.1 times on a long run basis, which for credit ratings agency purposes equates approximately to net debt to EBITDA of 1.5 times. The difference between these two ratios is primarily due to the capitalisation of operating leases by credit ratings agencies.

As at 31 December 2011, Telecom had been assigned a credit rating of A-/Stable by Standard & Poor's and A3/Stable by Moody's Investor Services.

On-market buyback

During the 2012 calendar year Telecom intends implementing an on-market share buyback of up to NZ$300 million.

The buyback will return capital, which is deemed surplus to existing requirements, and will result in a gearing ratio more consistent with Telecom's long-term capital management policy.

Ordinary dividends

For FY12 Telecom will continue with its existing dividend policy, to target a payout ratio of approximately 90% of adjusted net earnings, subject to there being no material adverse changes in circumstances or operating outlook.

In FY12 Telecom has shifted to paying dividends on a semi-annual basis. In accordance with this approach, a dividend of 9.0 cents per share has been declared for H1 FY12. The dividend will be fully imputed (at a ratio of 28/72) in line with the corporate income tax rate.

Subject to there being no adverse change in operating outlook, the dividend for H2 FY12 will be set to reflect the full year expected payout ratio. It is currently anticipated that the H2 FY12 dividend will be imputed in the range of 70 to 100%, although this prediction is highly sensitive to a number of factors. To the extent that dividends are not fully imputed, the amount of any supplementary dividend declared will be reduced on a pro-rata basis.

First half ordinary dividends	
Ordinary shares	9.0 cents
American Depositary Shares [1]	US 37.53 cents
"Ex" dividend dates	
New Zealand Stock Exchange	21 Mar 2012
Australian Stock Exchange	19 Mar 2012
New York Stock Exchange	20 Mar 2012
Books closing dates	
New Zealand, Australian Stock Exchanges	23 Mar 2012
New York Stock Exchange	22 Mar 2012
Payment dates	
New Zealand, Australia	5 Apr 2012
New York	13 Apr 2012

[1] Based on an exchange rate at 7 February 2012 of NZ$1.00 to US$0.8339 and a ratio of five ordinary shares per one American Depositary Share. The actual exchange rate used for conversion is determined in the week prior to payment when the Bank of New York performs the physical currency conversion.

Dividend Reinvestment Plan

The Dividend Reinvestment Plan has been restored after it was suspended during FY11 due to the UFB process. For the H1 FY12 dividend, shares issued under the Dividend Reinvestment Plan will be issued at the prevailing market price of ordinary shares. The last date for shareholders to elect to participate in the Dividend Reinvestment Plan for the H1 FY12 dividend is 23 March 2012.

Telecom intends to acquire an equivalent number of ordinary shares on-market, in order to eliminate an increase in capital arising from the plan. These mechanisms will be reviewed at each dividend date.

Competition, regulation and litigation

The significant changes in Telecom's competitive and regulatory environment in H1 FY12 are set out below.

This should be read in conjunction with the competitive and regulatory disclosures, as set out in Telecom's 2011 Annual Report, as well as the comparative section in the H2 FY11 Management Commentary, both of which are available online at:

http://investor.telecom.co.nz

Government's Ultra-Fast Broadband ('UFB') Initiative

The UFB initiative has the objective of increasing broadband speeds through deployment of fibre to the premises to 75% of the New Zealand population by 2019, with priority users reached by 2015. The Government will contribute NZ$1.35 billion, via Crown Fibre Holdings Limited ('CFH'), the Crown entity overseeing the Government's UFB initiative to selected participants in 33 national regions. In May 2011, Telecom's bid to participate in the Government's UFB initiative was accepted by CFH and Telecom was awarded 24 out of the 33 candidate areas.

In order to participate in the UFB initiative, subject to certain necessary approvals, Telecom had to demerge into two listed entities, being:

- **Chorus**, which owns and operates New Zealand's nationwide fixed line access network infrastructure, and comprises the Chorus business unit and certain parts of Telecom Wholesale; and

- **Telecom**, a retail-focused telecommunications business comprising fixed, mobile and ICT businesses.

More information about the UFB initiative can be found online at: http://investor.telecom.co.nz.

This demerger was successfully executed on 30 November 2011.

Telecommunications (TSO, Broadband and Other Matters) Amendment Act 2011

The Telecommunications (TSO, Broadband, and Other Matters) Amendment Act 2011 (the 'Telecommunications Amendment Act') establishes a substantially revised regulatory regime.

The Telecommunications Amendment Act:

- Revokes and replaces the 'three box' operational separation of Telecom prior to demerger with two separate demerged entities;
- Triggers a number of changes to the pricing of certain legacy copper services that Telecom provided before demerger, but which have now been transferred to Chorus;
- Implements the Government's TSO reforms;
- Provides for a review of the obligations under the TSO to be commenced and completed in 2013; and
- Provides for a review of the telecommunications regulatory framework, to be commenced no later than 30 September 2016 and, with best endeavours, to complete the review no later than 31 March 2019.

Operational separation undertakings (Undertakings)

On successful completion of the demerger, operational separation and all migration milestones under the operational separation undertakings across all parts of Telecom were revoked.

Chorus Open Access Deeds of Undertaking

As part of the new regulatory framework, Chorus was required to give three open access deeds of undertakings: The Copper, Fibre and Rural Broadband Initiative undertakings.

The open access deeds of undertakings collectively govern the way in which services must be provided by Chorus on its networks. The main cumulative effects of the deeds are that:

- Chorus is required to supply most services that it offers in accordance with a statutory principle of non discrimination;
- Chorus is required to build, supply and consume a small number of layer 1 'input services' on an equivalence of inputs ('EOI') basis;
- There are protections on customer commercial information and commercial information;
- There are positive requirements on Chorus to supply UBA with voice access as a bundle;
- There are requirements on Chorus to publish standard terms contracts in respect of fibre services;
- There are obligations on Chorus to develop a compliance framework including provision of information to the Commission, self reporting and the development of key performance indicators to demonstrate that EOI and non discrimination obligations are being met; and
- There are obligations on Chorus to prepare a plan within 12 months of demerger as to the ending of the sharing arrangements between Telecom and Chorus.

Chorus' compliance, EOI and non-discrimination obligations will continue to affect Telecom; however, the obligations contained in these deeds reside with Chorus.

Telecommunications services obligations

The Telecommunications Amendment Act implemented a number of TSO policy changes first announced by the Government in 2009, and confirmed in March 2010, including amendments to the methodology used to assess the net cost of complying with the TSO. The Government has stated that, based on this new methodology, it estimates Telecom's loss from meeting the TSO to be zero. On successful completion of the demerger, Telecom's obligations under the TSO were split between Telecom and Chorus as follows:

- Chorus is required to maintain lines and coverage obligations; and
- Telecom is required to provide retail services at the capped retail prices.

The Government is required, under the Telecommunications Amendment Act, to commence a comprehensive review of the TSO at or before the start of 2013. This review will take into account, amongst other things, changes to the telecommunications sector that have arisen from the rollout of new infrastructure and facilities and the impact of this on the TSO arrangements, the continued need and relevance of the TSO arrangement, the practicality of adopting a universal service obligation (rather than a provider-specific TSO arrangement), the impact of the TSO funding arrangements and related regulatory issues. The review is required to be completed by the end of 2013. There is no guarantee or certainty of the outcome with respect to any of the items covered within the TSO review.

The Telecommunications Amendment Act also introduced the Telecommunications Development Levy ('TDL'), which is an industry levy of $50 million per year between FY10 and FY16 and $10 million each year thereafter (adjusted for CPI) to be paid by certain market participants (termed 'liable persons') annually in arrears. The levy can be used to pay for any TSO charges, non-urban telecommunication infrastructure, upgrades to emergency calling and other wide purposes so long as a consultation process is followed. The amount payable by each liable person (including Telecom) will be determined by the Commerce Commission based on the proportion of revenue that each liable person receives from telecommunications services offered by means of a public telephone network.

Other regulatory matters

UCLL and SLU pricing

From 1 December 2011, Chorus has responsibility for providing the regulated UCLL and SLU services. Telecom cannot purchase these services from Chorus for three years after demerger. During that three year period, Telecom will instead purchase a number of other services from Chorus, many of which will have prices that are referenced directly to the regulated averaged UCLL and SLU prices.

UCLL and SLU prices are currently de-averaged; however, the Telecommunications Amendment Act requires that the prices be geographically averaged three years after demerger date (ie, 1 December 2014). The Commerce Commission was responsible for determining the averaged UCLL and SLU prices using a benchmarked methodology before demerger date. The Commerce Commission set prices at $24.46 and $14.77 per month respectively by applying a simple average of existing de-averaged prices. The Commission has subsequently initiated a further benchmarking review to consider whether the benchmark set used to calculate the existing de-averaged and averaged UCLL and SLU prices should be updated. The Commission is expected to release an issues paper on this matter shortly.

UBA pricing

UBA purchased with a phone service: The Telecommunications Amendment Act also required that the price for UBA services be 'frozen' for existing instances of UBA at the lower of the price on demerger date and the price that applied under the UBA standard terms determination at 30 June 2011. That price is $21.46 per month. From three years after demerger date, the UBA price will transition to a cost-based pricing methodology.

The initial pricing principle that the Commerce Commission must apply in calculating a cost-based price requires that it add the price of the averaged UCLL / SLU services to a benchmarked assessment of any 'additional costs' required to create the UBA service. The benchmark must be conducted using prices in comparable countries that use a forward-looking cost-based pricing method. While the cost based price will not apply until three years from the demerger date, the Commerce Commission must make reasonable efforts to review the UBA standard terms determination within twelve months of the demerger date. A pricing review using the price of the averaged UCLL / SLU services plus TSLRIC of the 'additional costs' to create UBA will also be available.

UBA purchased without a phone service (Naked UBA): In contrast, the Telecommunications Amendment Act required that, from demerger, all instances of Naked UBA would reflect the averaged UCLL and SLU prices.

Introduction of Chorus' Unbundled Copper Low Frequency Service ('UCLFS') and Baseband Service

In order to meet its TSO requirements, Chorus has announced plans to make available a technology neutral voice input service on a commercial basis. This service is known as Baseband. The pricing of a subset of the Baseband service – UCLFS (a voice input service offered over the copper access network) – was determined by the Commerce Commission in November 2011 (at the same time as averaged prices for UCLL and SLU were determined). The price for UCLFS was set at the averaged UCLL price ($24.46 per month).

Trans-Tasman mobile roaming

The Ministry of Economic Development ('MED') and the Australian Department of Broadband, Communications and the Digital Economy have announced a joint investigation into trans-Tasman mobile roaming pricing. The agencies will prepare a draft decision that outlines their market assessment and the options for joint action in the event of a market failure being determined. These options may include regulatory intervention. The two governments are likely to release a draft report in the first half of 2012.

111 Emergency services review

The Government is reviewing the 111 emergency calling service to ensure that it operates in a framework which accommodates changing technologies, practices and industry structures, while providing certainty about the governance framework. The MED is to undertake the review. The MED released a discussion paper on 10 February 2012 requesting comments by 30 March 2012. Further consultation will take place throughout the review.

Spectrum

The Minister of Telecommunications has confirmed 112MHz of spectrum will be available in the 700MHz spectrum range (694 - 806MHz) (the Digital Dividend) for new uses when television becomes fully digitalised. The MED is expected to hold a spectrum auction later in 2012. The rules of that auction are expected to be determined later this year.

Commerce Act litigation

The proceeding brought by the Commerce Commission under section 36 of the Commerce Act in relation to Telecom's implementation and maintenance of high speed data transmission service pricing remains active. Telecom has appealed the High Court decision which found that, although most of Telecom's pricing was not anti-competitive, the pricing of two tail circuits between March 2001 and late 2004 breached section 36. The Commerce Commission has cross appealed the points decided in Telecom's favour. A penalty hearing took place in December 2010, and a reserve judgment was delivered on 19 April 2011 ordering that Telecom pay a pecuniary penalty of $12 million. Telecom has paid this penalty but has also appealed the penalty judgment to the Court of Appeal. An appeal hearing for liability was held from 26 September to 3 October 2011, with the judgment reserved. The penalty hearing was heard on 21 November 2011, with the judgment reserved.

The proceeding commenced by the Commerce Commission in relation to Telecom's introduction of the 0867 service under section 36 of the Commerce Act was concluded with the delivery of the Supreme Court judgment on 1 September 2010, following a hearing in June 2010. The Supreme Court dismissed the Commerce Commission's appeal from the lower Courts' finding that Telecom had not breached section 36, and ordered the Commerce Commission to pay Telecom costs of $50,000 in the Supreme Court. The Commerce Commission has paid all Court costs and the matter is now closed.

Telecommunications Act litigation

Certain ongoing litigation was allocated between Chorus and Telecom. The allocated party will manage the allocated litigation at their cost, with indemnities in place to ensure that the party to which they are allocated bears the economic risk of that litigation. The following two matters were allocated to Chorus. The Separation Deed provides that claims under the indemnities must exceed a certain minimum claim amount and (other than those in relation to litigation) be brought before 30 June 2014. In addition, the amount payable under the indemnities and other claims under the Separation Deed is limited to $300 million.

TSO:

On 2 August 2011 Telecom and Vodafone announced that they had entered a full and final settlement of the various proceedings that they had initiated in relation to the Commerce Commission's TSO determinations for FY04, FY05, FY06, FY07 and FY08. The terms of the settlement are confidential to the parties. The settlement followed the Supreme Court hearing in February 2011 of Telecom and Vodafone's appeals in respect of the determinations for FY04, FY05, and FY06. The Supreme Court has issued a judgment in respect of the appeals, dismissing each of Telecom and Vodafone's appeals as moot, and dismissing the Commerce Commission's appeal in respect of the FY05 and FY06 determinations. Any residual issues in these matters are allocated to Chorus under the demerger Asset Allocation Plan and subject to the terms of a Separation Deed between Telecom and Chorus.

Sub Loop Extension Service and Sub Loop Unbundling:

A settlement of this matter was entered into in October 2011 between Telecom, the Commerce Commission, Vodafone, Kordia, Orcon, Callplus, Airnet and Compass, pursuant to which the total sum of $31.6 million was paid by Telecom (but recorded in the discontinued operations results) to compensate the various service providers, in agreed amounts. Any residual issues arising out of this matter are allocated to Chorus under the demerger Asset Allocation Plan and subject to the terms of a Separation Deed between Telecom and Chorus.

Other litigation

As noted in the 2011 Annual Report, a Notice of Proposed Adjustment ('NOPA') to Telecom's 2008 New Zealand tax return had been received from the Inland Revenue Department ('IRD'). Telecom responded, rejecting the IRD's NOPA. However, in February 2012 the IRD and Telecom agreed to settle the dispute based on confidential terms.

Telecom has other ongoing claims, investigations and inquiries, none of which it currently believes are expected to have significant effect on the financial position or profitability of Telecom.

Telecom cannot reasonably estimate the adverse effect (if any) on Telecom if any of the foregoing outstanding claims or inquiries are ultimately resolved against Telecom's interests. There can be no assurance that such cases will not have a significant effect on Telecom's business, financial position, and results of operations or profitability.

Future expectations

Telecom currently expects the following outcomes for the six month period ending 30 June 2012 ('H2 FY12'):

- H2 FY12 adjusted EBITDA of around NZ$560 million;
- H2 FY12 adjusted net earnings after tax of NZ$160 million to NZ$190 million; and
- H2 FY12 capital expenditure of approximately NZ$190 million to NZ$220 million.

This outlook is based on the current environment and economic, market and competitive conditions, which may change over time. Accordingly, this outlook is subject to material change. Telecom's ability to achieve this outlook is subject to risks. Further details on Telecom's risk factors are included in Telecom's 2011 Annual Report, available at: http://investor.telecom.co.nz

Forward-looking statements and disclaimer

This management commentary includes forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995 regarding future events and the future financial performance of Telecom. Such forward-looking statements are based on the beliefs of management as well as on assumptions made by and information currently available at the time such statements were made.

These forward-looking statements can be identified by words such as 'anticipate', 'believe', 'estimate', 'expect', 'intend', 'will', 'plan', 'may', 'could' and similar expressions. Any statements in this announcement that are not historical facts are forward-looking statements. These forward-looking statements are not guarantees or predictions of future performance, and involve known and unknown risks, uncertainties and other factors, many of which are beyond Telecom's control, and which may cause actual results to differ materially from those projected in the forward-looking statements contained in this management commentary. Factors that could cause actual results or performance to differ materially from those expressed or implied in the forward-looking statements are discussed herein and also include Telecom's anticipated growth strategies, Telecom's future results of operations and financial condition, economic conditions in New Zealand and Australia; the regulatory environment in New Zealand; competition in the markets in which Telecom operates; risks related to the demerger and operating as two separate companies, other factors or trends affecting the telecommunications industry generally and Telecom's financial condition in particular and risks detailed in Telecom's filings with the U.S. Securities and Exchange Commission. Except as required by law or the listing rules of the stock exchanges on which Telecom is listed, Telecom undertakes no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.

The securities referred to in this announcement have not been, and will not be, registered under the United States Securities Act of 1933 or under the securities laws of any state or other jurisdiction of the United States. This announcement does not constitute an offer of securities in the United States or to any person to whom it would not be lawful outside Australia and New Zealand. Any securities described herein may not be offered or sold in the United States absent registration under the Securities Act or pursuant to an applicable exemption from registration, or to any person to whom it would not be lawful outside Australia and New Zealand.

Non-GAAP financial measures

Telecom results are reported under IFRS. This management commentary includes non-GAAP financial measures which are not prepared in accordance with IFRS. The non-GAAP financial measures used in this presentation include:

1. EBITDA. Telecom calculates EBITDA by adding back (or deducting) depreciation, amortisation, finance expense/(income), share of associates' (profits)/losses and taxation expense to net earnings/(loss) from continuing operations.

2. Adjusted EBITDA. Adjusted EBITDA excludes significant one-off gains, expenses and impairments.

3. Capital expenditure. Capital expenditure is the additions to property, plant and equipment and intangible assets, excluding goodwill and other non-cash additions that may be required by IFRS such as decommissioning costs.

4. ARPU. Telecom calculates ARPU as revenue for the period (for mobile this is only voice and data) divided by an average number of customers.

5. Free cash flow. Free cash flow is defined as continuing and discontinuing EBITDA less capital expenditure.

6. Adjusted free cash flow. Adjusted free cash flow utilises adjusted EBITDA rather than underlying EBITDA defined above.

7. Adjusted net earnings. Adjusted net earnings are net earnings for the year adjusted by the same items to determine adjusted EBITDA, together with any adjustments to depreciation, amortisation and financing costs, whilst also allowing for any tax impact of those items.

Telecom believes that these non-GAAP financial measures provide useful information to readers to assist in the understanding of the financial performance, financial position or returns of Telecom, but that they should not be viewed in isolation, nor considered as a substitute for measures reported in accordance with IFRS. Non-GAAP financial measures as reported by Telecom may not be comparable to similarly titled amounts reported by other companies.

Glossary

The following terms included in this management commentary have the following meanings:

'ARPU'	Average Revenue per User (or Customer)
'Baseband'	Chorus Layer 2 product that enables service providers to offer voice services over fibre when copper is no longer available
'CFH'	Crown Fibre Holdings Limited
'Chorus'	Chorus, representing the discontinued operations of the Chorus and regulated Wholesale business owned by Telecom until demerger on 30 November 2011
'DSL'	Digital Subscriber Line, a family of communications technologies allowing high-speed data over existing copper-based telephony plant in the local loop
'EBITDA'	Earnings Before Interest, Tax, Depreciation and Amortisation
'EOI'	Equivalence Of Inputs
'EPS'	Earnings Per Share
'ESP'	Emergency Service Providers
'FCA'	Full Cost Apportionment
'FNT'	Fixed Network Transformation
'FMO'	Future Mode of Operation
'FTE'	Full Time Equivalent head count
'FTTN'	Fibre To The Node
'FY'	Financial Year ended 30 June
'GAAP'	Generally Accepted Accounting Principles
'ICT'	Information and Communication Technologies
'IFRS'	International Financial Reporting Standards
'IRU'	Indefeasible Right of Use in relation to network capacity
'ISDN'	Integrated Services Digital Network, a switched network providing end-to-end digital connectivity for simultaneous transmission of voice and/or data
'MED'	Ministry of Economic Development
'MVNO'	Mobile Virtual Network Operator
'NGN'	Next Generation Network
'NGT'	Telecom's Next Generation Telecommunications business model
'NM'	Not Meaningful
'PSTN'	Public Switched Telephone Network, a nationwide dial-up telephone network used, or intended for use, in whole or in part, by the public for the purposes of providing telecommunication between telephone devices
'H1 FY11'	Half Year Ended 31 December 2010
'H2 FY11'	Half Year Ended 30 June 2011
'H1 FY12'	Half Year Ended 31 December 2011
'RBI'	Rural Broadband Initiative
'SLES'	Sub Loop Extension Service
'SLU'	Sub Loop Unbundling
'SMS'	Short Message Service
'SMW3'	South East Asia Middle East Western Europe 3, an optical submarine telecommunications cable linking those regions
'Southern Cross' or 'SX'	The Southern Cross Cables Group which consists of two sister companies Southern Cross Cables Holdings Limited and Pacific Carriage Holdings Limited
'STD'	Standard Terms Determination
'TDL'	Telecommunications Development Levy
'TSO'	Telecommunications Service Obligation recorded in the Telecommunications Service Obligation Deed for Local Residential Telephone Service between the Crown and Telecom New Zealand Limited, dated December 2001
'UBA'	Unbundled Bitstream Access
'UCLFS'	Unbundled Copper Low Frequency Service
'UCLL'	Unbundled Copper Local Loop
'UFB'	Ultra-Fast Broadband
'VDSL'	Very High Speed Digital Subscriber Line
'VoIP'	Voice over Internet Protocol, a term used in IP telephony for managing the delivery of voice information using the IP
'WACC'	Weighted Average Cost of Capital

Telecom Group

Adjusted Group result

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1 FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m
Adjusted operating revenues and other gains					
Local service	507	497	486	469	457
Calling	518	485	479	449	394
Interconnection	83	95	100	95	53
Mobile	426	400	405	420	445
Data	319	307	291	283	268
Broadband and internet	256	255	250	237	238
IT services	234	252	274	287	267
Resale	147	131	124	111	93
Other operating revenue	133	105	114	85	97
Other gains	-	27	14	13	10
Adjusted operating revenues and other gains	**2,623**	**2,554**	**2,537**	**2,449**	**2,322**
Adjusted operating expenses					
Labour	439	419	421	411	411
Intercarrier costs	493	464	490	449	379
Other operating expenses	1,253	1,193	1,139	1,076	1,044
Adjusted operating expenses	**2,185**	**2,076**	**2,050**	**1,936**	**1,834**
Adjusted EBITDA - continuing operations	**438**	**478**	**487**	**513**	**488**
Adjusted EBITDA - discontinued operations	434	414	381	420	321
Adjusted EBITDA - total	**872**	**892**	**868**	**933**	**809**

Telecom Group

Group revenue & cost breakdown

	H1 FY10	H2 FY10	H1 FY11	H2 FY11	H1 FY12
Calling					
National - $m	310	294	281	263	238
International - $m	184	170	180	165	139
Other - $m	24	21	18	21	17
	518	485	479	449	394
Broadband and internet					
Broadband revenue - $m	229	224	226	216	219
Internet revenue - $m	27	31	24	21	19
	256	255	250	237	238
IT Services Revenue					
Procurement - $m	93	103	99	123	96
Professional Services - $m	17	20	20	20	20
Managed Services - $m	118	121	150	140	147
Other - $m	6	8	5	4	4
Total IT Services - $m	234	252	274	287	267
Southern Cross Dividends - $m	44	19	39	32	26
Other Operating Expenses					
Mobile Cost of Sales - $m	168	130	126	117	153
Other Cost of Sales - $m	140	152	164	169	155
Chorus related costs - $m	514	500	465	498	417
Other operating expenses - $m	431	411	384	292	319
	1,253	1,193	1,139	1,076	1,044
FTE Permanent - continuing operations	8,087	8,112	7,555	7,695	7,416
FTE Contractors - continuing operations	640	605	703	620	446
FTE Total - continuing operations	8,727	8,717	8,258	8,315	7,862
Basic EPS	13	7	9	-	52
Basic EPS (Adjusted)	13	7	8	12	12
Dividend per share declared	12.0	12.0	7.0	13.0	9.0

Telecom Group

Adjusted revenue and adjusted EBITDA by Unit

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1 FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m
Adjusted operating revenue and other gains					
Wholesale & International	482	482	527	501	387
Retail	1,049	1,027	1,012	1,003	962
Gen-i	722	727	714	708	683
AAPT	571	538	477	423	370
T&SS	306	297	305	284	279
Corporate	94	66	91	87	107
Revenue from Chorus discontinued operations	21	25	29	22	21
Eliminations	(622)	(608)	(618)	(579)	(487)
	2,623	2,554	2,537	2,449	2,322
Adjusted EBITDA					
Wholesale & International	78	86	75	70	79
Retail	176	230	240	253	233
Gen-i	99	124	105	132	123
AAPT	68	69	46	44	40
T&SS	-	(2)	-	4	1
Corporate	17	(29)	21	10	12
Continuing operations	438	478	487	513	488
Discontinued operations	434	414	381	420	321
Total group adjusted EBITDA	872	892	868	933	809

Telecom

Financial breakdown by business unit - Wholesale & International

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m
Adjusted operating revenues and other gains					
Local service	93	99	107	111	117
Calling	124	116	136	126	103
Interconnection	64	75	80	78	35
Mobile	4	6	4	2	2
Data	43	42	42	49	49
Broadband and internet	1	1	1	-	-
Other operating revenue	13	12	13	11	10
Internal revenue	140	131	144	124	65
Other gains	-	-	-	-	6
	482	482	527	501	387
Adjusted operating expenses					
Labour	21	20	20	18	12
Intercarrier costs	195	189	226	207	140
Other operating expenses	19	15	21	19	8
Internal expenses	169	172	185	187	148
	404	396	452	431	308
Adjusted EBITDA	**78**	**86**	**75**	**70**	**79**

The financial results of Wholesale & International represent, and have been restated for, continuing operations only and exclude certain regulated Wholesale results that have been allocated to discontinued operations.

Appendix – Supplemental information and KPIs

Analysis & KPI's - Wholesale & International

	H1 FY10	H2 FY10	H1FY11	H2 FY11	H1 FY12
Local Service					
Access Lines (000)	352	374	402	414	417
Calling					
National - $m	9	7	7	7	5
International - $m	113	107	128	117	96
Other - $m	2	2	1	2	2
	124	116	136	126	103
Analysis of international calls:					
International calling revenue comprised:					
International outward revenue - $m	7	8	8	8	7
International inward revenue - $m	13	7	6	5	4
International transits revenue - $m	93	92	114	104	85
	113	107	128	117	96
International calling minutes comprised:					
International outward minutes (m)	79	84	83	114	98
International inward minutes (m)	181	113	101	87	78
International transits minutes (m)	1,385	1,379	1,418	1,266	1,248
	1,645	1,576	1,602	1,467	1,424
International calling - average revenue per minute:					
International outward revenue per minute (cents)	8.86	9.52	9.64	7.02	7.14
International inward revenue per minute (cents)	7.18	6.19	5.94	5.75	5.13
Analysis of international transits:					
International transit revenue - $m	93	92	114	104	85
International intercarrier costs - $m	79	71	96	88	67
Gross margin - $m	14	21	18	16	18
Average margin per minute (cents)	1.01	1.52	1.27	1.26	1.44
Interconnect Revenues					
PSTN & Other interconnection - $m	31	33	33	30	28
Mobile to mobile interconnection - $m	33	42	47	48	7
	64	75	80	78	35
Broadband and internet					
Broadband revenue - $m	1	1	1	-	-
Other Operating Expenses					
Mobile Cost of Sales - $m	2	(1)	-	-	1
Other operating expenses - $m	17	16	21	19	7
	19	15	21	19	8
FTE Permanent	375	349	340	333	171
FTE Contractors	14	12	6	9	2
FTE Total[1]	389	361	346	342	173

[1] 50 FTEs related to regulated Wholesale have been removed from the prior comparative periods H1 FY10 to H2 FY11.

Telecom

Financial breakdown by business unit - Retail

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m
Adjusted operating revenues and other gains					
Local service	345	333	320	305	296
Calling	170	158	155	147	134
Mobile	308	286	296	313	328
Data	11	11	10	9	9
Broadband and internet	142	147	150	150	158
IT services	6	8	6	5	4
Other operating revenue	9	13	14	13	11
Internal revenue	58	58	61	61	22
Other gains	-	13	-	-	-
	1,049	1,027	1,012	1,003	962
Adjusted operating expenses					
Labour	82	80	75	72	66
Intercarrier costs	-	-	-	-	26
Other operating expenses	239	195	185	157	218
Internal expenses	552	522	512	521	419
	873	797	772	750	729
Adjusted EBITDA	**176**	**230**	**240**	**253**	**233**

Analysis & KPI's - Retail

	H1 FY10	H2 FY10	H1FY11	H2 FY11	H1 FY12
Local Service					
Access Lines (000)	1,191	1,146	1,099	1,061	1,023
Calling					
National - $m	126	119	119	113	103
International - $m	32	30	28	26	23
Other - $m	12	9	8	8	8
	170	158	155	147	134
Analysis of national calls:					
National calling revenue comprised					
National - $m	49	50	50	49	46
Mobile - $m	69	62	62	58	52
National 0800 - $m	8	7	7	6	6
	126	119	119	113	103
National calling minutes comprised					
National (m)	597	578	590	574	549
Mobile (m)	196	184	180	175	166
National 0800 (m)	24	22	22	21	20
	817	784	792	770	735
National calling - average revenue per minute					
National (cents)	8.21	8.65	8.47	8.54	8.38
Mobile (cents)	35.20	33.70	34.44	33.14	31.33
National 0800 (cents)	33.33	31.82	31.82	28.57	30.00
Analysis of international calls:					
International outward revenue - $m	32	30	28	26	23
International outward minutes (m)	187	172	165	159	152
International outward revenue per minute (cents)	17.11	17.44	16.97	16.35	15.13

Appendix – Supplemental information and KPIs

Analysis & KPI's - Retail (continued)

	H1 FY10	H2 FY10	H1 FY11	H2 FY11	H1 FY12
Mobile (Retail & Gen-i)					
Mobile revenue:					
Voice revenue - $m	222	205	208	207	202
Data revenue - $m	127	127	135	137	146
Other mobile revenue - $m	57	48	48	66	90
	406	380	391	410	438
Mobile call minutes (m)	758	701	698	675	658
Mobile call minutes per user per month	56	52	54	52	55
Mobile call price per minute (cents)	29.29	29.24	29.80	30.67	30.70
New Zealand average revenue per user ('ARPU')					
ARPU - $ per month	26.40	24.84	26.87	26.64	29.18
Postpaid - $ per month	54.85	51.79	54.79	54.11	55.59
Prepaid - $ per month	8.95	8.79	9.52	9.63	10.29
Voice - $ per month	16.81	15.32	16.32	16.05	16.91
Data - $ per month	9.60	9.52	10.54	10.59	12.26
Number of mobile customers at period end (000) (New Zealand- Group)					
Postpaid	859	840	829	830	857
Prepaid	1,431	1,312	1,347	1,249	1,157
Internal postpaid	20	19	16	18	17
Total mobile customers (CDMA & XT)	2,310	2,171	2,192	2,097	2,031
XT Postpaid (000)	267	369	518	607	723
XT Prepaid (000)	200	343	492	576	669
Total XT customers (000)	467	712	1,010	1,183	1,392
Data only devices (000) (Retail & Gen-i)	101	133	143	173	191
Broadband and internet					
Broadband revenue - $m	132	137	142	144	153
Internet revenue - $m	10	10	8	6	5
	142	147	150	150	158
Broadband connections (000)	559	579	580	591	598
Dial up connections (000)	107	93	82	73	64
IT Services Revenue					
Procurement - $m	-	-	1	1	-
Other - $m	6	8	5	4	4
Total IT Services - $m	6	8	6	5	4
Other Operating Expenses					
Mobile Cost of Sales - $m	127	92	90	83	117
Other Cost of Sales - $m	8	2	4	3	3
Other operating expenses - $m	104	101	91	71	98
	239	195	185	157	218
FTE Permanent	2,036	2,197	2,004	1,840	1,740
FTE Contractors	166	109	101	137	123
FTE Total	2,202	2,306	2,105	1,977	1,863

Telecom

Financial breakdown by business unit - Gen-i

Gen-i Total	**H1 FY10 NZ$m**	**H2 FY10 NZ$m**	**H1FY11 NZ$m**	**H2 FY11 NZ$m**	**H1 FY12 NZ$m**
Adjusted operating revenues and other gains					
Local service	54	53	50	48	44
Calling	84	80	75	75	68
Mobile	98	94	95	97	110
Data	193	181	168	147	140
Broadband and internet	12	11	11	8	8
IT services	228	244	268	282	263
Resale	3	3	2	2	1
Other operating revenue	16	10	7	7	6
Internal revenue	34	47	38	42	39
Other gains	-	4	-	-	4
	722	727	714	708	683
Adjusted operating expenses					
Labour	167	160	171	162	156
Intercarrier costs	-	-	-	1	5
Other operating expenses	217	224	230	218	214
Internal expenses	239	219	208	195	185
	623	603	609	576	560
Adjusted EBITDA	**99**	**124**	**105**	**132**	**123**

Appendix – Supplemental information and KPIs

Financial breakdown by business unit - Gen-i (continued)

The following is a break down of Gen-i into Telecommunication and IT solutions

Telecommunication solutions	H1 FY10 NZ$m	H2 FY10 NZ$m	H1 FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m
Adjusted operating revenues and other gains					
Local service	54	53	50	48	44
Calling	84	80	75	75	68
Mobile	98	94	95	97	110
Data	193	181	168	147	139
Broadband and internet	12	11	11	8	8
IT services	20	15	31	27	26
Resale	3	3	2	2	1
Other operating revenue	13	7	6	6	5
Internal revenue	20	25	28	27	20
Other gains	-	4	-	-	-
	497	473	466	437	421
Adjusted operating expenses					
Labour	92	90	91	84	72
Intercarrier costs	-	-	-	1	5
Other operating expenses	84	69	83	62	66
Internal expenses	235	214	202	187	174
	411	373	376	334	317
Adjusted EBITDA	**86**	**100**	**90**	**103**	**104**

IT solutions	H1 FY10 NZ$m	H2 FY10 NZ$m	H1 FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m
Adjusted operating revenues and other gains					
Data	-	-	-	-	1
IT services	208	229	237	255	237
Other operating revenue	3	3	1	1	1
Internal revenue	14	22	10	15	19
Other gains	-	-	-	-	4
	225	254	248	271	262
Adjusted operating expenses					
Labour	75	70	80	78	84
Other operating expenses	133	155	147	156	148
Internal Expenses	4	5	6	8	11
	212	230	233	242	243
Adjusted EBITDA	**13**	**24**	**15**	**29**	**19**

Appendix – Supplemental information and KPIs

Analysis & KPI's - Gen-i

	H1 FY10	H2 FY10	H1 FY11	H2 FY11	H1 FY12
Local Service					
Access Lines (000)	82	80	78	76	74
Calling					
National - $m	67	65	60	59	56
International - $m	7	5	6	5	5
Other - $m	10	10	9	11	7
	84	80	75	75	68
Analysis of national calls:					
National calling revenue comprised					
National - $m	9	11	8	6	6
Mobile - $m	32	28	28	26	24
National 0800 - $m	26	26	24	27	26
	67	65	60	59	56
National calling minutes comprised					
National (m)	143	139	143	142	109
Mobile (m)	128	121	128	124	124
National 0800 (m)	297	289	301	303	292
	568	549	572	569	525
National calling - average revenue per minute					
National (cents)	6.29	7.91	5.59	4.23	5.50
Mobile (cents)	25.00	23.14	21.88	20.97	19.35
National 0800 (cents)	8.75	9.00	7.97	8.91	8.90
Analysis of international calls:					
International outward revenue - $m	7	5	6	5	5
International outward minutes (m)	27	25	25	23	25
International outward revenue per minute (cents)	25.93	20.00	24.00	21.74	20.00
Broadband and internet					
Broadband revenue - $m	12	11	11	8	8
Broadband connections (000)	19	19	19	19	19
IT Services Revenue					
Procurement - $m	93	103	98	122	96
Professional Services - $m	17	20	20	20	20
Managed Services - $m	118	121	150	140	147
Total IT Services - $m	228	244	268	282	263
Other Operating Expenses					
Mobile Cost of Sales - $m	39	39	36	34	35
Other Cost of Sales - $m	132	150	160	166	152
Other operating expenses - $m	46	35	34	18	27
	217	224	230	218	214
FTE Permanent - Telcommunication solutions	1,187	1,172	1,102	1,072	880
FTE Permanent - IT solutions	1,588	1,554	1,556	1,580	1,448
Total FTE Permanent	2,775	2,726	2,658	2,652	2,328
FTE Contractors - Telcommunication solutions	52	72	78	47	25
FTE Contractors - IT solutions	148	153	241	199	119
Total FTE Contractors	200	225	319	246	144
FTE Total	2,975	2,951	2,977	2,898	2,472

Appendix – Supplemental information and KPIs

Telecom

Financial breakdown by business unit - AAPT

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1 FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m	H1 FY10 A$m	H2 FY10 A$m	H1 FY11 A$m	H2 FY11 A$m	H1 FY12 A$m
Adjusted operating revenues and other gains										
Local service	15	12	9	5	-	12	9	8	3	-
Calling	140	131	113	101	89	112	103	88	76	70
Interconnection	19	20	20	17	18	16	15	15	14	14
Mobile	16	14	10	8	5	13	11	8	6	4
Data	72	73	71	78	70	57	54	56	59	55
Broadband and internet	101	96	88	79	72	82	79	70	59	56
Resale	144	128	122	109	92	114	102	95	82	71
Other operating revenue	9	21	4	-	2	9	16	3	-	2
Internal revenue	55	43	40	26	22	43	35	32	19	17
	571	538	477	423	370	458	424	375	318	289
Adjusted operating expenses										
Labour	88	84	75	74	64	70	66	59	54	51
Intercarrier costs	298	275	264	241	208	239	216	207	182	162
Other operating expenses	85	81	61	41	38	68	67	48	30	29
Internal expenses	32	29	31	23	20	25	23	23	19	16
	503	469	431	379	330	402	372	337	285	258
Adjusted EBITDA	**68**	**69**	**46**	**44**	**40**	**56**	**52**	**38**	**33**	**31**

Analysis & KPI's - AAPT

	H1 FY10 A$m	H2 FY10 A$m	H1 FY11 A$m	H2 FY11 A$m	H1 FY12 A$m
Local Service					
Consumer access Lines (000)	227	199	n/a	n/a	n/a
Calling					
National - A$m	95	89	74	63	58
International - A$m	17	14	14	13	12
	112	103	88	76	70
Broadband and internet					
Broadband revenue - A$m	68	62	57	48	45
Internet revenue - A$m	14	17	13	11	11
	82	79	70	59	56
Consumer broadband connections (000)	120	113	n/a	n/a	n/a
Other Operating Expenses - A$m	68	67	48	30	29
	68	67	48	30	29
FTE Permanent	1,166	1,120	882	781	768
FTE Contractors	53	40	34	9	14
FTE Total	1,219	1,160	916	790	782

Telecom

Financial breakdown by business unit - T&SS

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1FY11 NZ$m	H2FY11 NZ$m	H1FY12 NZ$m
Adjusted operating revenues and other gains					
Other operating revenue	5	3	4	5	14
Internal revenue	301	284	287	271	265
Other gains	-	10	14	8	-
	306	297	305	284	279
Adjusted operating expenses					
Labour	53	48	53	55	62
Other operating expenses	152	137	150	116	123
Internal expenses	101	114	102	109	93
	306	299	305	280	278
Adjusted EBITDA	**-**	**(2)**	**-**	**4**	**1**

Analysis & KPI's - T&SS

	H1 FY10	H2 FY10	H1FY11	H2FY11	H1FY12
FTE Permanent	1,516	1,481	1,430	1,843	1,766
FTE Contractors	200	209	225	206	117
FTE Total	1,716	1,690	1,655	2,049	1,883

Telecom

Financial breakdown by business unit - Corporate

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1FY11 NZ$m	H2 FY11 NZ$m	H1 FY12 NZ$m
Adjusted operating revenues and other gains					
Other operating revenue	60	21	43	27	33
Internal revenue	34	45	48	55	74
Other gains	-	-	-	5	-
	94	66	91	87	107
Adjusted operating expenses					
Labour	28	27	27	30	51
Other operating expenses	27	41	27	27	26
Internal expenses	22	27	16	20	18
	77	95	70	77	95
Adjusted EBITDA	**17**	**(29)**	**21**	**10**	**12**

Analysis & KPI's - Corporate

	H1 FY10	H2 FY10	H1FY11	H2 FY11	H1 FY12
Southern Cross Dividends - $m	44	19	39	32	26
FTE Permanent	219	239	241	246	643
FTE Contractors	7	10	18	13	46
FTE Total	226	249	259	259	689

Telecom

Discontinued operations

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1FY11 NZ$m	H2FY11 NZ$m	H1FY12 NZ$m
Adjusted operating revenues and other gains					
Local service	9	13	13	13	13
Data	5	7	8	10	9
Broadband and internet	41	42	40	54	44
Other operating revenue	14	9	14	17	13
Internal revenue	514	500	465	498	417
	583	571	540	592	496
Adjusted operating expenses					
Labour	18	17	18	19	17
Other operating expenses	110	115	112	131	137
Internal expenses	21	25	29	22	21
	149	157	159	172	175
Adjusted EBITDA[1]	**434**	**414**	**381**	**420**	**321**

Analysis & KPI's - Discontinued operations

FTE Permanent	263	281	308	312	-
FTE Contractors	11	17	7	13	-
FTE Total	274	298	315	325	-

[1] Before demerger/refinancing costs

Telecom Group

Capex Summary (Continuing & Discontinued Operations)

	H1 FY10 NZ$m	H2 FY10 NZ$m	H1 FY11 NZ$m	H2 FY11 NZ$m	H1FY12 NZ$m
Transformation and regulation					
XT mobile network	29	71	63	44	42
FTTN	78	74	68	68	40
FNT	42	23	7	1	-
Retail NGT	47	62	40	25	23
Separation	92	71	57	34	12
UFB	-	-	-	-	43
RBI	-	-	-	-	11
Other Regulatory	5	2	2	3	1
Total transformation and regulation	293	303	237	175	172
Business sustaining					
IT systems	22	47	29	26	25
Gen-i	18	41	37	29	20
AAPT	24	53	39	17	18
Southern Cross capacity	33	15	-	4	1
Network maintenance and growth	87	118	73	111	55
New products and services	7	40	29	32	11
Other business sustaining	16	66	36	40	23
Total business and sustaining	207	380	243	259	153
Total Group	500	683	480	434	325

Capital expenditure is presented on an accruals basis