FINANCIAL COMMENTARY

Air New Zealand's normalised earnings[1] before taxation for the first six months of the 2014 financial year were $180 million, an increase of 29 percent over the previous corresponding period. Statutory earnings before taxation were $197 million, while net profit after taxation was $140 million, up 40 percent. The result demonstrates continued earnings growth underpinned by a strong operating performance.

Dividend Payment	4.5 cents per share
Dividend Record Date	14 March 2014
Dividend Payment Date	21 March 2014

REVENUE

Operating revenue was $2.3 billion, a decrease of $38 million or 1.6 percent on the previous corresponding period. This was driven by a $49 million decrease from foreign exchange movements. Excluding the negative impact of foreign exchange, operating revenue was up $11 million or 0.5 percent on a 1.3 percent reduction in capacity.

Passenger revenue excluding the impact of foreign exchange increased by $45 million, or 2.4 percent to $1.93 billion due to improved load factors, up 1.1 percentage points to 84.3 percent, and stronger local currency yields. Foreign exchange had a $43 million negative impact on passenger revenue during the period, due to the New Zealand dollar being stronger against the airline's major trading currencies.

International long haul yields were up 0.8 percent on a 4.9 percent decrease in capacity, which was primarily driven by withdrawals from the Hong Kong-London and Auckland-Osaka routes. Excluding the impact of foreign exchange, yields were up 3.7 percent. Demand was down 2.5 percent and load factor increased 2.2 percentage points to 86.0 percent due to network realignment.

Tasman and Pacific Island routes saw both capacity and demand increases of 2.4 percent, with capacity growth being driven partly by the up-gauge to B777-200 aircraft on the Auckland-Perth and Auckland-Honolulu routes. Load factor was flat at 83.3 percent for the period, while yield declined 2.7 percent due to the relative strength of the New Zealand dollar against the Australian dollar.

Capacity on the Domestic network increased by 4.1 percent, driven by the introduction of new A320 aircraft replacing the smaller B737-300, and additional ATR72-600 aircraft entering service. Load factor decreased by 0.1 of a percentage point to 81.0 percent. Yield reduced by 0.6 percent during the period, due to pricing reductions to stimulate demand, which increased by 4.0 percent.

Cargo revenue for the first six months of the 2014 financial year was $148 million, a decrease of $16 million or 10 percent on the previous corresponding period. Excluding the impact of foreign exchange, Cargo revenue was down by $13 million or 8 percent. This result was driven by a 3 percent reduction in volume (revenue tonne kilometres) as a result of withdrawing from the Hong Kong-London route, as well as a yield decline of 5 percent.

Contract Services revenue was $132 million, down 11 percent from $149 million in the previous corresponding period. The reduction was due to less third party engineering activity undertaken. Other revenue was $118 million, down $7 million or 5.6 percent.

EXPENSES

Operating expenditure decreased by $92 million for the period, a 4.8 percent improvement which includes reduced costs due to foreign exchange movements and a net gain on non-hedge accounted and ineffective derivatives that hedge exposures in other financial periods. Excluding the above factors, operating expenditure improved 1.6 percent on a Group wide capacity decrease of 1.3 percent and flat demand.

Labour costs were $566 million compared to $530 million in the previous corresponding period, an increase of $36 million or 6.8 percent. This was due to a combination of rate increases, redundancy costs incurred in the current period of $14 million relating to cabin crew and wide body maintenance, as well as pilot and cabin crew training costs of $10 million as the Group transitions to operating new fleet types. Headcount remained unchanged.

Fuel costs improved by $61 million due to lower prices and improving fleet efficiencies, combined with reduced activity. Excluding net gains and losses on derivatives that hedge exposures in other periods, fuel costs were down $46 million. The average US dollar into plane cost excluding hedge timing was 5 percent lower than the previous corresponding period.

Air New Zealand's fuel hedging programme resulted in gains totalling $10 million, compared to losses of $12 million in the previous corresponding period.

Aircraft maintenance and overhaul costs were $135 million for the period, a decrease of $12 million or 8.2 percent. This was primarily due to reduced materials costs on third party maintenance work.

Aircraft operations costs were $216 million, a decrease of $1 million or 0.5 percent compared with a decrease in available seat kilometres of 1.3 percent. Increased landing charges and air navigation costs were offset by savings in Cargo ground handling costs and foreign exchange.

Passenger services expenses were $109 million, compared to $117 million in the previous corresponding period. This was driven by reduced ground handling costs resulting from a change in supplier, and savings from ongoing business transformation initiatives.

Other expenses reduced by $16 million during the period, reflecting a continued focus on cost improvements, combined with the prior period including the Commerce Commission settlement.

Fleet replacement programmes resulted in increased depreciation and reduced lease costs as owned aircraft replaced operating leased aircraft. The residual values of exiting fleets were reassessed, resulting in increased depreciation expenses.

Net finance costs were down $6 million on the previous corresponding period, with interest revenue higher due to increased cash holdings and improved rates, combined with lower average debt costs.

FOREIGN EXCHANGE IMPACT

The impact of a stronger New Zealand dollar relative to Air New Zealand's major trading currencies resulted in a negative foreign exchange movement of $30 million on both revenue and cost base, offset by a positive movement from the hedging programme.

Overall, currency movements had a $1 million favourable impact on the Group result.

CASH AND FINANCIAL POSITION

Net cash at the end of the period was $1.13 billion, $22 million lower than at 30 June 2013, due to ongoing investment in new aircraft and further investment in Virgin Australia.

The Group had strong operating cashflows of $300 million for the period, including an increase of $68 million of tax paid.

Net gearing, including capitalised operating leases, was 43.9 percent.

[1]Normalised Earnings

Normalised earnings represents earnings stated in compliance with NZ IFRS (Statutory Earnings) after excluding net gains and losses on derivatives that hedge exposures in other financial periods. Normalised earnings is a non-IFRS financial performance measure that matches derivative gains or losses with the underlying hedged transaction, and represents the underlying performance of the business for the relevant period. Normalised earnings is reported within the condensed Group interim financial statements and is subject to review by the Group's external auditors.