

Special Talking Water

Thursday 13 October 2016



Murray Irrigation

Murray Irrigation financial results 2015/16

Murray Irrigation has finalised its financial statements for 2015/16 which show a small operational profit despite the low allocation and low volume of deliveries.

This result was achieved by cutting operational costs and tightening processes to minimise losses without compromising service.

Murray Irrigation made a commitment to customers at last year's Annual General Meeting that it would utilise three levers to bring the business back to a breakeven status – cost, volume and price.

Pivotal to this commitment is the principle to address costs as a priority before reviewing our pricing structures and commercial opportunities available to the business.

During the year, Murray Irrigation has been able to cut \$3.5 million from its operational expenses through new procedures, more strategic maintenance and increased accountability. This enabled Murray Irrigation to report a profit at EBITDA (earnings before interest, tax, depreciation and amortisation); however, the impact of depreciation has again resulted in a loss at operating EBIT.

This shows that we have our operating expenditure at an appropriate level to achieve breakeven status, but the impact of depreciation makes achieving a neutral EBIT difficult.

Compounding this issue, a recent business review found that the book value of our assets exceeded the current depreciated replacement cost. In other words, our assets are overvalued for their current use. This is in a large part due to the reduction in the long-term average delivery volume through the Murray Irrigation system as a result of the Murray Darling Basin Plan and previous government water reform. To date, over 27 percent of our original licenced entitlements are now held by environmental water managers.

According to Australian Accounting Standards (AASB 136), if the value of a company's assets exceeds the recoverable amount, or 'value in use', then the company must undertake an impairment test.

The valuation of Company assets was undertaken by an independent consultancy firm who considered the replacement cost, whether the same network would be created if it was replaced today, how much technology and efficiencies had changed, industry practices and comparable events. The consultancy firm found that the value of the Company's assets in the accounts did exceed its recoverable amount which meant that an impairment was required.

By impairing our assets, Murray Irrigation is realising a loss in the value of our assets in this year, which is shown in our financial statements as a provisional adjustment. This in turn will result in lower depreciation expense in future years improving our future EBIT earnings.

Reducing the asset burden in our financial accounts will reduce the need to factor those costs into our revenue requirements which are met through the fees and prices we charge our customers.

Murray Irrigation will release the full 2015/16 financial reports with the Annual Report, which will be accessible online later this month.

The following page provides answers to some frequently asked questions about impairment and the impact on Murray Irrigation.

Murray Irrigation will make a detailed presentation on our financial results at the Annual General Meeting to be held on Thursday 17 November at the Deniliquin Golf Club at 7pm. Customers will receive meeting notice papers and a summary of the financial results in the mail in the coming week.

Michael Renehan
Chief Executive Officer

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Frequently asked questions

What is impairment?

Impairment is a standard accounting practice, *AASB 136 Impairment and Assets*, to recognise where a company's asset is valued above the amount that it can be expected to recover through use or sale. In Australia, an impairment can be reversed in the event of a revised recoverable valuation.

Is impairment necessary?

Under Australian Accounting Standards, a company must conduct an impairment test if the carrying value of their assets exceeds the value in use. If the entity is not-for-profit, the recoverable amount is referred to as '*value in use*'. For specialised assets, such as water infrastructure assets, *value in use* equates to the depreciated replacement cost of the asset.

What does it mean for Murray Irrigation?

Murray Irrigation's non-financial assets are significant and the value attributed to them affects not only the Company's reported financial position, but also our reported performance. Therefore it is important that the assets are valued correctly on our books.

Murray Irrigation contracted Deloitte to conduct an independent assessment of the value of its assets taking into account replacement value, current technology, and standard industry practice. This valuation found a fair value of \$191,980,000, calculated using the depreciated replacement cost method, against a written down book value in our accounts of \$266,823,932.

Realising an impairment now will reduce future depreciation improving the Company's EBIT into the future. This in turn will reduce the need to factor those costs into our revenue requirements met through the fees and prices we charge our customers.

Why has the value of Murray Irrigation assets changed?

One of the factors considered by valuers is; if you were to build the system today, would you build it to the same specifications?

Utilisation of Murray Irrigation infrastructure has changed significantly since it was designed and constructed. The system is capable of delivering around 1,500GL per year (long-term average) and prior to the Millennium drought was delivering an average of 1,000GL/yr. Through ongoing water reform, Murray Irrigation customers and shareholders now hold over 27 percent less entitlements against Murray Irrigation's bulk licence than at the time of privatisation. The current expectation is that our long term average water delivery on farm will be in the vicinity of 600GL per year. This means our assets are underutilised compared to their design capacity.

What does impairment mean for Murray Irrigation customers?

The impairment is a write-down in the book value of assets only. It does not change the purpose or use of those assets. It will have no impact on Murray Irrigation's day-to-day operations at all.

Long term, however, the reduced impact of asset value and depreciation on our reported financial position will show an improvement in the Company's finances. This in turn will reduce the need for the Company to recover those costs through our fees and charges. The expected outcome is that Murray Irrigation will be better positioned to manage costs and the associated impact on fees and charges.

Can the impairment be reversed?

Yes, in Australia it is possible to reverse the impairment of an asset where the asset's recoverable amount has been reassessed and is shown to be higher than the impaired book value.