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ASX & Media Release

Asset impairment and recognition of onerous contracts

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AGL Energy Limited (AGL) has today announced it intends to recognise charges of $2,686 million (post-tax) in its financial statements for the period ended 31 December 2020. These charges reflect $1,920 million in provisions for onerous contracts related primarily to legacy wind farm offtake agreements, increases to environmental restoration provisions of $1,112 million, and further impairments of $532 million across AGL's Generation Fleet and Natural Gas assets, net of a positive tax effect of $878 million.

These charges follow an accelerated deterioration to long-term wholesale energy market forecasts in recent months, reflecting policy measures to underwrite new build of electricity generation and lower technology costs, leading to expectations of increased supply. As a result, the long-term outlook for wholesale electricity and renewable energy certificates now indicates a sustained and material reduction in prices.

Combined with sharp reductions in near-term wholesale energy prices as a result of challenging macro-economic conditions, and the outcomes of AGL's three-yearly review of environmental restoration provisions substantially completed in recent weeks, this has reduced the valuation of AGL's Generation Fleet cash generating unit. The impairment of the Natural Gas assets is a direct result of the increase in environmental restoration provisions. The carrying value of other AGL cash generating units is unchanged.

AGL Managing Director & CEO, Brett Redman, said: "As Australia's largest energy retailer and largest generator of electricity, we continue to see material opportunities for AGL to participate in the energy transition as customer needs, community expectations and technology evolve. Notwithstanding these charges, our broad and diverse portfolio of electricity generation assets will continue to have a vital role to play in enabling the transition of the energy system."

The provisions for onerous contracts of $1,920 million (pre-tax) relate primarily to long-term wind offtake agreements which AGL entered into between 2006 and 2012 to support the development of the renewables sector at that time. These offtake agreements were entered at prices significantly higher than spot and forecast prices for electricity and renewable energy certificates today.

The increase in environmental restoration provisions of $1,112 million comprises $799 million from a reduction in the discount rate used to derive the present value of future estimated restoration cash flows from 10 percent to 3 percent, and $313 million from an increase in estimated future expenditure following the substantial completion of the three-yearly review of long-term rehabilitation requirements.

The further impairments, primarily to the carrying value of property, plant and equipment (PP&E) and goodwill, reflect the impacts of the outlook for long-term wholesale energy market conditions across AGL's coal and gas generation plant, legacy Natural Gas production assets and other minor assets.

AGL will recognise charges noted in this release as a Significant Item against Statutory Profit in its financial statements for the period ended 31 December 2020. AGL anticipates the accounting changes will have an immaterial impact on Underlying Profit after tax (which excludes Significant Items) in the financial year ending 30 June 2021 (FY21). As a result, AGL's guidance range for FY21 Underlying Profit after tax is unchanged from the range of $500 million to $580 million provided on 21 December 2020.

AGL anticipates a positive impact to Underlying Profit after tax in FY22 and FY23 from the above changes of approximately $50 million to $80 million. These impacts are the aggregate of a decrease in cost of goods sold as a result of the provision for the onerous wind farm offtake contracts, a net decrease in depreciation expense, and a net increase in interest costs.

Authorised for release by AGL's Board of Directors.

Further enquiries

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About AGL

Proudly Australian for more than 180 years, AGL supplies around 4.2 million energy and telecommunications customer services. We're committed to becoming a leading multi-product retailer, making energy and other essential services simple, fair and transparent. AGL operates Australia's largest private electricity generation portfolio within the National Electricity Market, comprising coal and gas-fired generation, renewable energy sources such as wind, hydro and solar, batteries and other firming technology, and gas production and storage assets. We are building on our history as Australia's leading private investor in renewable energy to now lead the business of transition to a low emissions, affordable and smart energy future in line with the goals of our Climate Statement. We have a passionate belief in progress and a relentless determination to make things better for our communities, customers, the Australian economy and our planet.

Appendix

The following tables set out the changes in assessed carrying value in the Generation Fleet cash generating unit and Natural Gas assets.

The remainder of AGL's cash generating units are not shown, as indicators of impairment were not present and therefore carrying value re-assessment was not undertaken as part of the 31 December 2020 financial statements preparation.

All estimates are subject to the finalisation of AGL's half-year report for the period ended 31 December 2020.

Table 1: increase in environmental restoration provision

($m)	Generation Fleet	Natural Gas	Combined impact
Prior carrying value	7,610	455	
Environmental restoration – cash flows	225	88	313
Environmental restoration – discount rate	704	95	799
Environmental restoration – total	929	183	1,112
Carrying value post increase to restoration provision	8,539	638	

Table 2: impact of impairments on carrying value

($m)	Generation Fleet	Natural Gas	Combined impact (pre-tax)	Combined impact (post-tax)
Carrying value post increase to restoration provision	8,539	638		
Onerous contract provisions	(1,920)	-	(1,920)	(1,344)
Impairment – PP&E	(774)	(231)	(1,005)	(707)
Impairment – goodwill	(626)	-	(626)	(626)
Impairment - inventory	(13)		(13)	(9)
Carrying value post onerous provision/impairments	5,206	407		
Change in value	(3,333)	(231)	(3,564)	(2,686)
Tax benefit				878

Note: The increase in the environmental restoration provision has the effect of increasing the asset base before carrying value analysis is applied. As such, the gross impairment amount recognised in effect includes the full value of the increase in the environmental restoration provision. Net of the impact of this increase, the pre-tax impairment of other assets would be $532 million.