

BUSINESS EFFICIENCY

STRATEGIC GOALS

- > Increase business value through capital and operating efficiency and effective risk management
- > Improve efficiency through innovative asset management and business practices
- > Invest prudently and efficiently, taking account of environmental, social and financial considerations, whole-of-life costs, risks and service needs
- > Maximise resource efficiency by embracing innovation and collaborating with key stakeholders and strategic partners
- > Operate and maintain our assets efficiently, in accordance with sustainability principles
- > Earn a commercial return on assets to fund operations and investments and to pay shareholder dividends
- > Ensure investment decisions are sustainable
- > Maintain sound governance

KEY ACHIEVEMENTS

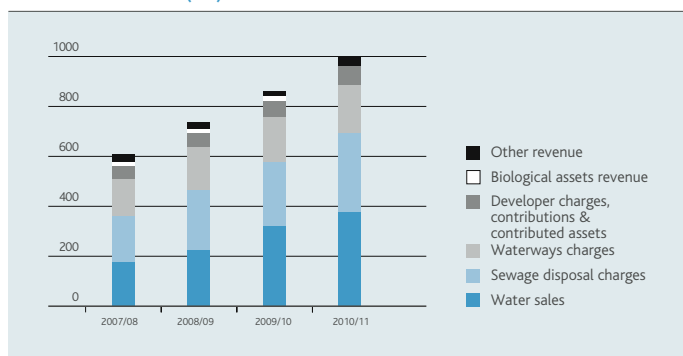
- > Delivered a net profit after tax of \$157.8 million
- > Successfully delivered \$753.1 million of capital works, mostly through our alliances
- > Cash returns to Government of \$173.1 million
- > Achieved 2011 'Overall Champion' Eco-Buy award for excellence in green purchasing
- > Completed a 5-star South East Regional Office building for the Waterways Group
- > Completed a joint legal services tender with the retail water businesses and appointed a new legal services panel
- > Replaced desktop computers with laptops and physical servers with 'virtual' servers, creating energy efficiencies

CHALLENGES

- > Clarifying regulatory requirements and customer priorities for our next Water Plan (2013/14 to 2017/18) particularly given the impending implementation of the Victorian Government's desalination plant
- > Demonstrating to the Government and ensuring that the delivery of the capital plan provides value for money
- > Continuing to achieve business efficiencies in the context of expenditure targets set in the Victorian Competition and Efficiency Commission review
- > Ongoing delivery of \$3.6 billion of capital works on time and within budget (for the five years ending June 2013)
- > Demonstrating operating efficiency to our stakeholders
- > Increasing number of insurance claims, particularly in relation to flooding events
- > Responding to the future potential impacts of carbon tax

Melbourne Water is delivering \$3.6 billion of infrastructure projects and programs in the five years ending in June 2013 through alliance contracts that provide commercial incentives for superior performance

OPERATING REVENUE (\$M)



STRONG FINANCIAL PERFORMANCE

This year, we made payments to the Victorian Government of \$173.1 million (compared with \$175.9 million in 2009/10). This consisted of \$26.5 million in dividends, income tax equivalent payments of \$116.7 million, a financial accommodation levy of \$26.8 million and local government rate equivalents of \$3.1 million. We also incurred expenditure to Government of \$14.2 million in land tax (\$13.8 million in 2009/10) and \$4.1 million in payroll tax (\$3.9 million in 2009/10).

Operating revenue was \$997.3 million (\$858.4 million in 2009/10). The key driver for the increase compared to last year is due to increased water, sewerage and drainage revenue resulting from higher prices and growth. This increase was partly offset by a reduction in water flows as a result of higher than average rainfall reducing demand. The increased revenue is being used to fund our capital works program.

Operating expenditure was \$783.3 million (\$619.8 million in 2009/10). The key drivers for the increase compared to last year are due to increased depreciation and amortisation expense as a result of implementation of fair value on infrastructure assets for the first time in 2009/10 as well as the increase in the capital program and increased finance costs due to increased borrowings to fund our capital works program.

Net profit after tax was \$157.8 million (\$186.4 million in 2009/10). This is mainly due to the increase in operating expenditure (primarily depreciation and finance costs) above the increase in operating revenue (primarily water, sewerage and drainage).

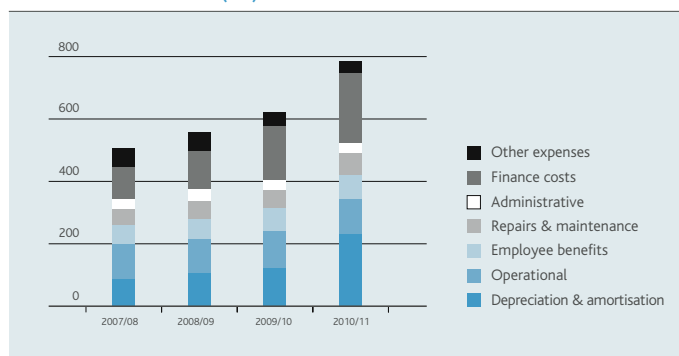
Total assets increased to \$9,754.5 million from \$8,948.3 million in 2009/10. The increase is mainly due to the investment of \$753.1 million (\$973.9 million in 2009/10) in capital works. Revaluation adjustments of \$225 million on land and buildings and \$16.1 million on infrastructure assets also contributed to the increase.

Total liabilities increased to \$5,379.7 million from \$4,929.8 million in 2009/10. The increase is mainly due to an increase in interest-bearing liabilities (borrowings) of \$547.4 million due to the funding required to deliver our capital program.

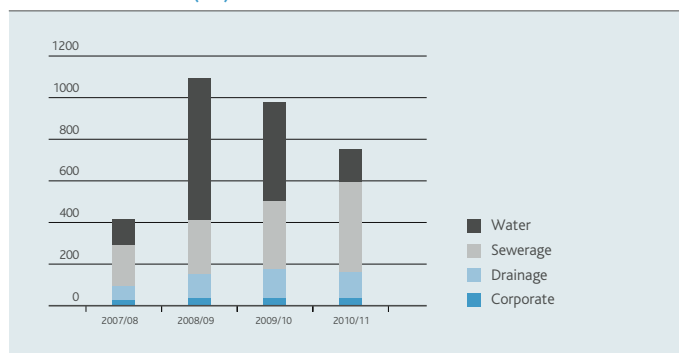
We achieved a return on equity (NPAT/Total Equity) of 3.6% compared with 4.6% in 2009/10, which was below our target of \geq 4.0%. This is mainly due to higher than planned equity balances following first time implementation of fair value on infrastructure assets at 30 June 2010.

Our gearing ratio (Debt/Debt + Equity) of 45.3% (43.3% in 2009/10) and our cash interest cover ratio of 2.8 times (3.4 times in 2009/10) were both within our target ranges.

OPERATING EXPENDITURE (\$M)



CAPITAL EXPENDITURE (\$M)



EFFICIENCY THROUGH COLLABORATION

Melbourne Water is delivering \$3.6 billion of infrastructure projects and programs in the five years ending in June 2013 through alliance contracts that provide commercial incentives for superior performance relating to cost, timing, social and environmental outcomes.

These alliances bring together skilled and experienced people from the design and construction industries to enhance innovation and increase efficiency.

This year, \$753.1 million of capital works was delivered through:

- Project teams working on the Melbourne Main Sewer Replacement, Northern Sewerage Project, Eastern Treatment Plant upgrade and the Cardinia Connection of the desalination plant to Melbourne Water's supply system

- Bundled projects through program alliances
- Minor works through maintenance service partners
- Other traditional project arrangements.

Strong governance is a key to the alliance model. This year, we continued a program of independent validation of project cost estimates; managed an audit program to ensure compliance with policy, procedures and agreed commercial terms; and administered a continual improvement program, performance/value reporting and post-project reviews.

Melbourne Water will work closely with its partners to deliver the remaining two years of capital projects in an efficient and effective manner.

The building incorporates rainwater harvesting for gardens and toilet flushing, solar panels, certified timber products and recycled materials, water sensitive landscaping and use of waste heat from the treatment plant for heating and cooling.



RESEARCH AND TECHNOLOGY

To ensure that Melbourne Water continues to provide high quality services, research and development is undertaken to enhance knowledge for strategic purposes and to improve efficiency through scientific excellence, innovation and the adoption of new technology.

Key initiatives in 2010/11 included:

- The discovery and development (in conjunction with Latrobe University) of a novel, naturally occurring virus that destroys the foam-producing bacteria, GALO, responsible for significant operational issues at the Eastern Treatment Plant
- The completion of the multi-agency Western Port Scientific Review which consolidated current knowledge about Western Port environmental issues and will be used to set future research projects
- Continued investigation of the presence and nature of the protozoan parasite *Cryptosporidium* in native and feral animals in our protected water supply catchments, the results of which support Melbourne Water's unfiltered status

- Involvement in the National Centre for Excellence for Recycled Water with a position on the Research Advisory Council and representation on a major project to set national validation guidelines for recycled water, aimed at ensuring science-based sensible guidance
- Implementation of a major research program aimed at better understanding the impact of toxicants including pesticides on aquatic ecosystems in waterways through a new research centre, the Victorian Centre for Aquatic Pollution Identification and Management, which opened in 2010.

New legal services panel

Melbourne Water appointed a new shared legal services panel with the retail water businesses in December 2010. The appointment of the panel has resulted in increased efficiency and value for money in procuring external legal services.

SUSTAINABILITY INVESTMENT

A new building for the Waterways South East Regional Office has been completed at Worsley Road in Bangholme, with the provision to house up to 80 staff. The building was occupied in February 2011.

This building has achieved a 5-star Green Star 'Design' certification from the Green Building Council of Australia (GBCA), which rates it in the 'Australian Excellence' category.

The building incorporates rainwater harvesting for gardens and toilet flushing, solar panels, certified timber products and recycled materials, water sensitive landscaping and use of waste heat from the treatment plant for heating and cooling.

Information technology improvements

Melbourne Water continues to implement initiatives to make its IT infrastructure more efficient and sustainable including:

- Replacement of desktop computers with laptops, which are more energy efficient. Laptops are about 30% more efficient than an equivalent desktop and 74% of the fleet has so far been replaced

Above: New Waterways South East Regional Office

- The replacement of physical servers with equivalent 'virtual' servers, creating efficiencies in both energy usage and maintenance costs. The first phase has seen 74 servers virtualised, with an efficiency gain of about 20%.

Excellence in green purchasing

Melbourne Water had great success at the 2011 ECO-Buy Awards, winning three awards including the overall champion for excellence in green purchasing.

This award recognises excellence in all five dimensions of sustainable procurement: people, policy, process, engaging suppliers and measurement, and is an indication of how highly regarded our sustainable procurement policy is viewed externally.