Core Income Portfolio

NZFUNDS

Manager insight – 31 January 2009

Throughout 2008, the Core Income Portfolio has been very defensively positioned with a high weighting to cash and short credit duration. This has shielded the Portfolio from the turmoil in global markets.

During December, the strategy changed to reduce the level of cash held in the Portfolio and increase the interest rate duration of the Portfolio. We have looked to achieve this while maintaining a high level of liquidity in the Portfolio.

In order to achieve the above changes, we added a number of Australian bank senior bond issues that are guaranteed by the Australian government. These issues are denominated in US and Australian dollars (hedged back to NZ dollars). One of the reasons we like these securities is that they provide significantly better yields (approx 1%) than government bonds of the same maturity – even though they have similar associated risk.

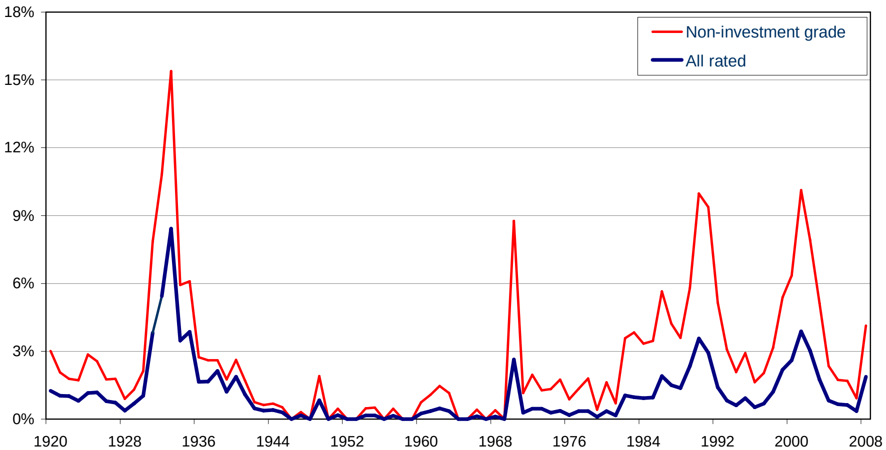
This allocation resulted in a strong finish to the year thanks to a sharp move lower in global interest rates. The portfolio performance was 1.10%[1] in December and 0.75%[1] in January.

Looking forward, we expect corporate defaults to increase significantly during 2009 and for markets to be unforgiving towards lower-rated issuers.

Consequently, our focus will be on owning a diversified portfolio of highly-rated corporate bonds that operate in defensive sectors – for example, Telecom and Fonterra – together with mortgages and direct bank loans via Titan bonds. This should hold investors in better stead than falling into the retail investor trap of only holding one or two corporate bonds.

Bond insight: Default cycle

Moody's annual issuer-weighted corporate default rates
1920-2008



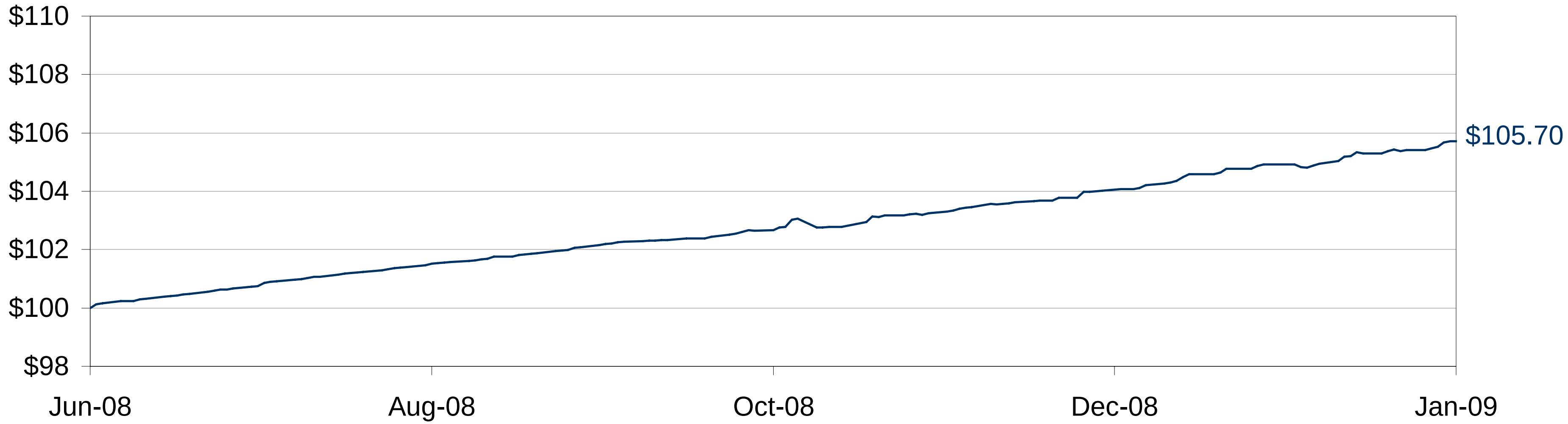
Source: Moody's.

[1] Returns are stated after fund fees and expenses, but before any advisory fees or investor tax. Past performance is not necessarily an indication of future returns.

Core Income Portfolio

Performance since 25 June 2008 to 31 January 2009

Performance attribution	One month	Three month	Six month
Positive	Long duration positions	-	-
Neutral	Credit spreads	-	-
Negative	n/a	-	-



One-month return	Three-month return	Six-month return	One-year return	Since inception of strategy pa
0.75%	2.44%	4.59%	-	-

Returns are stated after Portfolio fees and expenses, but before any advisory fees or investor tax. Past performance is not necessarily an indication of future returns. The Portfolio was launched on 20 May 2008. As the Portfolio was only invested on 25 June 2008, performance is measured from this date.

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Portfolio summary as at 22 January 2009

Portfolio summary

Number of securities	29*
Leverage utilised	Zero
Weighted average running yield (approximately)	6.6%**
Weighted average credit rating	AA-

Sector / Security	Value of portfolio	Proportion of portfolio	Maturity date / Expected average life date	S&P rating
Bank deposits / Bank bills		**36%**		
ANZ (Bank bills)	$7,341,358	15%	Apr-09	A1+
ASB Bank (Bank bills)	$2,101,618	4%	Apr-09	A1+
BNZ (Bank bills)	$3,106,154	6%	Mar-09	A1+
Kiwibank (Bank bills)	$1,876,158	4%	Apr-09	A1+
Westpac (Bank deposits)	$5,123	0%	Current	A1+
Westpac (Bank bills)	$3,537,498	7%	Apr-09	A1+
Corporate bonds		**14%**		
Telstra Corporation	$2,432,370	5%	Nov-12	A
Citigroup	$1,468,933	3%	May-12	A
Fonterra	$2,936,549	6%	Feb-09	A+
Governmnent guaranteed bonds		**25%**		
ANZ	$1,428,133	3%	Dec-10	AAA
Commonwealth Bank Australia	$3,852,067	8%	Dec-13	AAA
National Australia Bank	$1,439,227	3%	Jan-12	AAA
Westpac Bank	$5,858,282	12%	Dec-11	AAA
Residential mortgages		**12%**		
AMSNZ mortgage security (various issues)***	$4,590,074	9%	May-10 to Mar-11	AA- to AAA
Sapphire New Zealand mortgage security (various issues)	$1,337,398	3%	Feb-11 to Jul 11	AA
Other debt securities		**4%**		
Titan (portfolio of Australian & US corporate loans)	$1,960,108	4%	Jun-09	AA
Loans		**9%**		
Private Loan Trust (Fidelity - 32 current loans)	$4,749,227	9%	Jun-09	NR
Total	**$50,020,277**	**100%**		

*With reference to bank bills, the Portfolio often holds more than one security under a given issuer. The 'number of securities' takes this into account. **The running yield is stated After the deduction of management, custodial and trustee fees. The running yield is not the actual return of the fund, nor is it a projection or forecast. ***Originated and serviced by AMSNZ, a subsidiary of GE Capital. Note: Rounding may affect the subtotals and totals.

Notes

For further information or to request a copy of the relevant Investment Statement, please contact New Zealand Funds Management Limited.

Past performance is not necessarily an indication of future returns.

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