MANAGER INSIGHT – 30 APRIL 2010

This 'Manager insight' takes a closer look at one of the outstanding performers in the New Zealand share market over the last 18 months – Restaurant Brands. In April, the Portfolio had around 2% of its assets in Restaurant Brands.

Share insight: Restaurant Brands

While the name of the company may not be that familiar, the brands that make up its portfolio are Pizza Hut, Starbucks and KFC. Yet despite the quality of brands in its portfolio, Restaurant Brands saw its shares go as low as $0.59c in late October of 2008, driven by the sustained poor performance of different sectors of the underlying businesses.

The largest contributor to the company's earnings is KFC, which typically makes up more than 60% of total revenue and a larger share of profits. KFC's (or Kentucky Fried Chicken as it was still branded at that point) revenue remained broadly static for several years from the late 1990s into the mid 2000s, yet its costs rose inexorably and consequently, its margins suffered a sharp decline. By 2005, the segment's Earnings before Interest and Tax (EBIT) margins had declined to 12%, from as high as 17% just 4 years earlier. To the company's credit, they recognised the problem and instigated a very substantial and very successful turnaround. The business was rebranded to KFC and a major store refurbishment programme began. However, while the KFC turnaround strategy turned out to be extremely successful, it was initially obscured by problems elsewhere in the business. The company undertook a poorly judged expansion into Pizza Hut outlets in Victoria which ultimately proved both short-lived and expensive. Then, Pizza Hut in New Zealand began to underperform. Faced with the aggressive expansion of domestic pizza outlets like Hell and the well funded arrival of Domino's in the domestic market, Pizza Hut could not compete and posted operating earnings losses from 2007 to 2009.

The dire performance of Pizza Hut was worrying, but it had become apparent through 2007 and 2008 that the KFC turnaround programme was having a dramatic effect. The stores that had undergone refurbishment were seeing immediate substantial sales growth. Importantly, as the programme was rolled out to more stores, the effects were being reproduced and the initial stores were holding onto their sales – it wasn't the novelty factor but a step change in customer perception and demand. Moreover, it became clear that the scope of further growth was enormous as at that stage, only a relatively small number of stores had been refurbished. Finally, while the Pizza Hut losses were a concern, the risks were dramatically outweighed by the KFC upside potential. Consequently in mid 2008, the Portfolio took a significant position in Restaurant Brands around the 90c mark and has (largely) held it since. The stock remained out of favour and declined for a sustained period, yet the investment case remained compelling. Finally in early 2009, when it became clear that Pizza Hut sales had stabilised, the stock began to rally. Since then, it has risen to $2.36 and provided investors with a very tasty return. And with a dividend yield of 5.80%, based on a modest and easily sustainable payout, and continued prospects of strong growth, Restaurant Brands remains a key holding for this Portfolio.

TAX-ADJUSTED PERFORMANCE TO 30 APRIL 2010 FOR DIVIDEND YIELD COMPOSITE STRATEGY* (PART 1)

DYP PERFORMANCE ATTRIBUTION	1 MONTH	3 MONTH	6 MONTH
Positive	Air New Zealand	Mainfreight	Restaurant Brands
Neutral	The Warehouse	Fisher & Paykel Healthcare	Air New Zealand
Negative	Goodman Fielder	Goodman Fielder	The Warehouse

COMPARISON	DYP 1 MONTH	DYP 3 MONTH	DYP 6 MONTH	DYP 1 YEAR	COMPOSITE 2 YEAR PA	COMPOSITE 5 YEAR PA	COMPOSITE 7 YEAR PA	COMPOSITE SINCE INCEPTION[1]	COMPOSITE MAXIMUM DRAWDOWN[X]
Dividend Yield Composite Strategy*	1.61%	1.95%	-0.14%	10.44%	-2.39%	4.18%	9.35%	372.17%	-36.26%
Comparative index**	0.42%	2.77%	1.74%	14.09%	-2.13%	3.09%	6.69%	259.19%	-31.30%

[1] Pre-tax equivalent gross return. IMPORTANT: Please refer to the slide that follows for the footnotes relating to this slide

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TAX-ADJUSTED PERFORMANCE TO 30 APRIL 2010 FOR DIVIDEND YIELD COMPOSITE STRATEGY* (PART 2)

Tax-adjusted Performance

* The Dividend Yield Composite Strategy is a tax-adjusted composite strategy stated after portfolio fees and expenses, but before any advisory fees or investor tax. Past performance is not necessarily an indication of future returns.

Dividend Yield Composite Strategy

The Dividend Yield Composite Strategy is made up of the New Zealand Equity Trust (EIT) from 2 December 1992 to 6 June 2003, the Dividend Yield Fund (DYF) from 6 June 2003 to 28 February 2008, and the Dividend Yield Portfolio (DYP) data from 28 February 2008 onwards.

EIT was a New Zealand Unit Trust. DYF was established as an Australian Unit Trust. DYP is a PIE. The tax-adjusted composite strategy is designed to remove, as much as possible, the impact of the different tax regimes that applied during the calculation period. By doing so it enables the returns from EIT, DYF and DYP to be represented in a substantially consistent manner without tax distortions.

The Dividend Yield Composite Strategy covers five different tax regimes, and accordingly the use of different calculation methods is necessary to remove the impact of the various regimes. These are:

i) The period to 6 June 2003. New Zealand Unit Trust returns were reported net of tax and have been grossed up by 33% (being the tax rate applicable to New Zealand Unit Trusts) to reflect the pre-tax position.

ii) The period 6 June 2003 to 30 September 2005. Australian Unit Trust returns were generally not taxable to investors, and to provide a comparison the returns have been grossed up by 33% to reflect that actual returns were after tax.

iii) The period from 1 October 2005 to 31 March 2007. Investors were only taxable on distributions made by Australian Unit Trusts. The returns have therefore been grossed up by 33% and adjusted for any tax payable on distributions made.

iv) The period from 1 April 2007 to 28 February 2008. Australian Unit Trust holdings were subject to the Fair Dividend Rate regime. The returns have been grossed up by the tax amount payable under the Fair Dividend Rate regime.

v) The period from 28 February 2008. PIE returns are reported gross of tax, and as such no adjustment has been made to returns attributable to DYP.

This calculation is undertaken for comparative purposes only, and should not be confused with the portfolio return generated from either EIT, DYF or DYP. More details on these calculations, together with the formulae used, are available on request from New Zealand Funds Management.

TAX-ADJUSTED PERFORMANCE TO 30 APRIL 2010 FOR DIVIDEND YIELD COMPOSITE STRATEGY* (PART 3)

Comparative Index

** The comparative index is made up of 70% NZX50 Index and 30% 90-day bank bill rate. All index figures are sourced from Bloomberg. A fee of 0.60% pa has been deducted from the NZX50 Index to reflect the cost of obtaining a passive New Zealand share market exposure using an Exchange Traded Fund and the brokerage associated with purchasing it. A fee of 0.20% pa has been deducted from the 90-day bank bill rate as bank bills are usually accessed by retail investors through a managed fund. The 90-day bank bill rate has been included in the comparison because the mandate allows the manager to invest up to 30% of the Portfolio in cash and capital notes. The comparative index is stated on a pre-tax basis.

Maximum Drawdown

x Returns should be looked at in conjunction with the level of risk associated with an investment. For this reason, the 'maximum drawdown' is included for both the strategy and the comparison. The maximum drawdown is a measure of volatility and represents the largest decline in value experienced during the reporting period.

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COMPLETE PORTFOLIO AS AT 30 APRIL 2010

PORTFOLIO SUMMARY

Number of securities	26
Yield[1]	6.7%
Weighted average market cap (share holdings)	$12.6b
Cash, capital notes & other	15%
Shares	85%
Total economic exposure	100%

SECTOR / SECURITY	COUNTRY	PORTFOLIO VALUE	PORTFOLIO ALLOCATION	MARKET CAP (NZ$M)	PRICE/ EARNINGS	PRICE/ BOOK	PAYOUT RATIO	YIELD
CASH			**9.1%**					
Bank deposits / Bank bills	New Zealand	$1,498,339	9.1%	n/a	n/a	n/a	n/a	2.8%
CYCLICALS			**28.1%**					
Freightways	New Zealand	$1,146,837	6.9%	$496	16.4	3.1	76.0%	6.7%
The Warehouse	New Zealand	$1,135,402	6.9%	$1,151	13.4	0.8	78.0%	8.2%
Fletcher Building	New Zealand	$765,228	4.6%	$5,013	16.4	0.6	55.0%	4.7%
Mainfreight	New Zealand	$483,797	2.9%	$638	16.4	0.5	48.0%	4.0%
Hallenstein Glassons	New Zealand	$398,551	2.4%	$209	12.2	1.0	95.0%	9.5%
Air New Zealand	New Zealand	$380,701	2.3%	$1,388	15.4	0.7	70.0%	6.8%
Restaurant Brands	New Zealand	$314,918	1.9%	$225	10.8	0.5	52.0%	5.3%
Skellerup Holdings	New Zealand	$29,253	0.2%	$124	12.5	0.6	55.0%	6.4%
NON CYCLICALS			**56.6%**					
Trustpower	New Zealand	$1,142,804	6.9%	$2,315	19.2	1.6	93.0%	7.3%
Fisher & Paykel Healthcare	New Zealand	$782,506	4.7%	$1,824	3.6	6.6	95.0%	5.1%
Goodman Property	New Zealand	$774,725	4.7%	$850	11.0	1.0	93.0%	12.3%
Kiwi Income Property	New Zealand	$774,641	4.7%	$807	13.3	0.8	98.0%	10.7%
Goodman Fielder	New Zealand	$754,305	4.6%	$2,596	11.0	1.2	80.0%	7.0%
Coca Cola Amatil	Australia	$486,710	2.9%	$10,712	16.9	4.8	70.0%	3.5%
Spotless	Australia	$475,576	2.9%	$860	12.0	1.4	53.0%	4.4%
AMP NZ Office Trust	New Zealand	$399,035	2.4%	$758	12.5	0.8	96.0%	11.5%
Port of Tauranga	New Zealand	$389,082	2.4%	$936	20.1	1.4	79.0%	5.7%
Contact Energy	New Zealand	$387,822	2.3%	$3,763	22.0	1.2	96.0%	6.5%
Commonwealth Bank of Australia	Australia	$382,452	2.3%	$111,336	14.8	2.6	76.0%	4.8%
Auckland International Airport	New Zealand	$381,590	2.3%	$2,608	24.3	1.4	100.0%	5.9%
Westpac	New Zealand	$378,862	2.3%	$98,788	13.5	2.1	69.0%	4.7%
Foster's	Australia	$375,112	2.3%	$13,232	15.2	2.7	77.0%	4.2%
Sky City	New Zealand	$369,479	2.2%	$1,783	13.5	2.2	69.0%	7.0%
Metcash	Australia	$368,931	2.2%	$3,905	12.8	2.6	79.0%	5.1%
ANZ Banking Group	New Zealand	$365,261	2.2%	$96,902	13.1	1.8	64.0%	4.5%
STW Communications	Australia	$271,920	1.6%	$395	8.4	0.8	39.2%	4.7%
Photon Group	Australia	$85,189	0.5%	$254	5.5	0.5	42.1%	7.6%
UXC	Australia	$8,646	0.1%	$181	7.5	0.7	36.5%	4.9%
Corporate Express	Australia	$6,620	0.0%	$1,190	14.6	4.1	64.9%	4.5%
CAPITAL NOTES & OTHER			**6.2%**					
Kiwi Income Property MCNs	New Zealand	$754,273	4.6%	n/a	n/a	n/a	n/a	9.0%
Sky City Capital Notes	New Zealand	$279,052	1.7%	n/a	n/a	n/a	n/a	8.0%
TOTAL ECONOMIC EXPOSURE[2]		**$16,547,619**	**100.0%**					

[1] The yield calculation represents an estimate of the yield on the Portfolio, calculated using yields forecast by New Zealand Funds Management for each company's current financial year. Where applicable, the security's yield reflects the benefit derived from imputation credits received. The yield is not the return on the Portfolio, nor is it a projection or forecast. The Portfolio's return could be less than the Portfolio's yield. Details of the yield calculation are available on request from New Zealand Funds Management. [2] Total economic exposure represents the total economic value of a Portfolio, which is the gross asset value of the Portfolio adjusted for the effect of direct or indirect derivative positions taken by the Portfolio. Note: Rounding may affect the subtotals and totals.

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

Past performance is not necessarily an indication of future returns.