

Manager insight – 30 November 2009

The Portfolio produced a return of 0.64%¹ in November and 2.86%¹ year to date. The Portfolio's objective is to protect against inflation, which is currently running at 2.15%² for the first nine months of 2009. This is equivalent to 0.24% a month or 2.63% year to date. This month's 'Manager Insight' reviews the Portfolio's allocation to property.

“Don't wait to buy real estate, buy real estate and wait.”

Will Rogers (1935)

Property is an ideal addition to the Mid Term Growth Portfolio as its attributes align well with the Portfolio's objectives. First, it is a relatively stable investment. The rental stream property owners are entitled to provides steady income and price changes do not tend to be overly dramatic. Second, property tends to produce strong returns in periods of high inflation. Building prices and rentals appreciate strongly, driven by growth in the replacement cost of buildings (the determinant of prices in the long run) as the cost of building materials and labour rates increase.

The Portfolio accesses property by investing in listed property trusts. The strategy has two components – one focused on domestic listed property trusts and the other on international listed trusts. Listed property trusts trade on global share markets. This has both costs and benefits. The primary advantage of listed property trusts is that they trade like shares which means that these securities can be bought and sold using a broker in the same way as a normal share. This is a significant advantage when compared to the other form of property ownership – direct property

investment. Direct property investment has unreliable liquidity mechanisms. In simple terms, when markets are good there is usually a method to exit, but in difficult times this will not always be available.

This liquidity advantage comes at a cost. Listing property introduces price volatility. As the property trusts fall into and out of favour with the schizophrenic share market, their prices rise and fall. This turns a relatively stable investment into one that can have share market risk. To control this risk, a systematic hedging strategy is utilised. The objective of this strategy is to remove or hedge out the listed property exposure risk when share market risk has taken over. The method by which the hedging strategy is implemented is tailored to best suit the hedging instruments available. In the domestic component the property exposure is sold to manage risk. Two triggers are used to signal the timing for selling the listed trusts – one when listed property prices trend downward and the other when broking analysts' forecasts are downgraded (a signal of a difficult property market). The international component is hedged using derivatives and uses a combination of price trend signals.

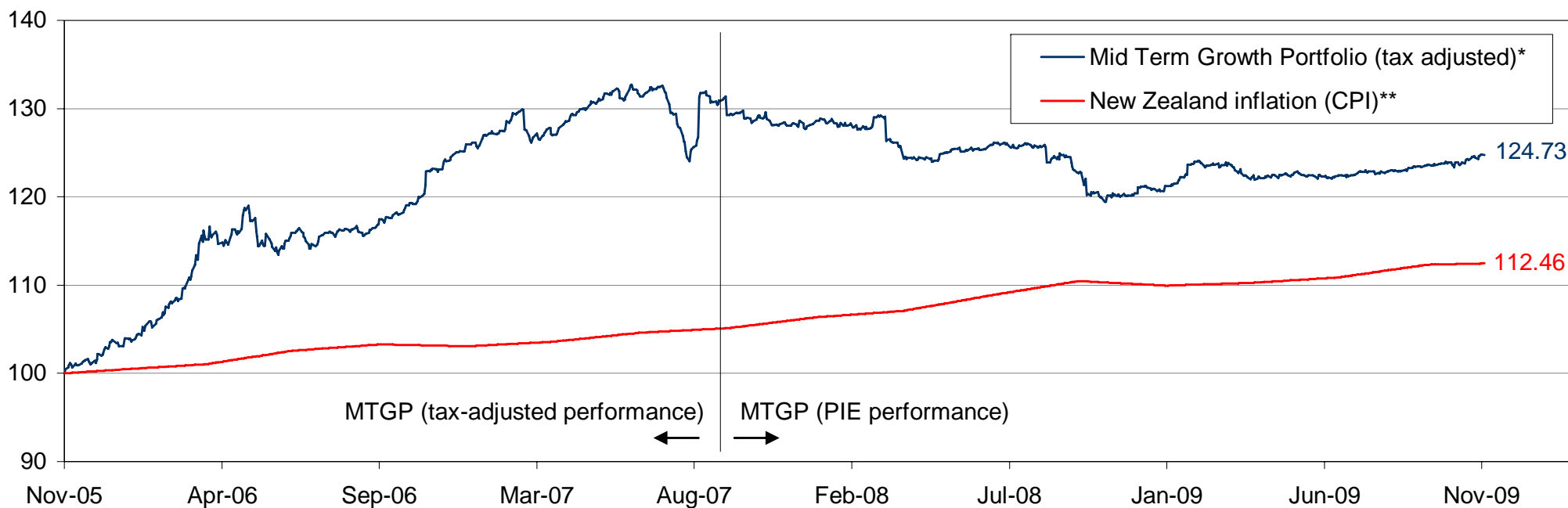
Another advantage of listed property is the quality of the underlying assets that can be acquired. To maximise this advantage, we outsource the selection of the international listed property trusts to specialist managers, Resolution Capital and Challenger/Heitman. These specialists carry out fundamental analysis on the underlying properties held by the listed trusts.

¹ 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. ² Source: Bloomberg.

Mid Term Growth Portfolio

Tax-adjusted performance since mandate change (3 November 2005) to 30 November 2009* (Part 1)

MTGP performance attribution	1 month	3 month	6 month
Positive	Equity manager alpha; bonds	Bonds; global shares	Bonds
Neutral	Cash	Cash	Global shares; cash
Negative	Global shares; property	Property	Equity manager alpha



Comparison	1 month	3 month	6 month	1 year	2 year pa	5 year pa	7 year pa	Since inception pa	Maximum drawdownx
Portfolio (tax adjusted)*	0.64%	1.52%	1.89%	3.58%	-1.31%	-	-	5.57%	-10.03%
New Zealand inflation**	0.07%	0.55%	1.62%	2.12%	3.02%	-	-	2.92%	-0.46%

IMPORTANT: Please refer to the slide that follows for the footnotes relating to this slide.

Tax-adjusted performance since mandate change (3 November 2005) to 30 November 2009* (Part 2)

Tax-adjusted performance

* Tax-adjusted performance for the Mid Term Growth Portfolio (MTGP) is 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 with its current mandate on 3 November 2005.

MTGP was established as a New Zealand Unit Trust (NZUT). In calculating the tax-adjusted performance for MTGP the return prior to 30 September 2007 has been 'grossed up' at 33% (being the tax rate applicable to a NZUT) to reflect that previously tax was paid within the trust. The tax-adjusted performance is designed to remove, as much as possible, the impact of the tax paid by the Portfolio during the calculation period. By doing so it enables the returns from MTGP to be represented in a substantially consistent manner throughout the measurement period.

The tax-adjusted performance covers two different tax regimes, and accordingly two different calculation methods are applied. The two calculation periods are:

- i) the period pre 30 September 2007 (being the period prior to the introduction of the PIE regime);
- ii) the period post 1 October 2007 (being the date from which MTGP was subject to the PIE regime).

This calculation is undertaken for comparative purposes only, and should not be confused with the return generated from the Mid Term Growth Portfolio.

More details on these calculations, together with the formulae used, are available on request from NZ Funds.

Comparative index

** The comparative index is New Zealand's inflation rate as measured by the Consumers Price Index. Source: Bloomberg.

Maximum drawdown

× Returns should be looked at in conjunction with the level of risk associated with an investment. For this reason, we have included the 'maximum drawdown' for both the Portfolio and the comparison. Maximum drawdown is a measure of volatility and represents the largest cumulative decline experienced during the reporting period.

Mid Term Growth Portfolio



Complete portfolio as at 30 November 2009

Portfolio summary

Yield ¹	5.7%
Income strategies (before share hedge)	58%
Growth strategies (before share hedge)	32%
Currency strategies	0%
Total economic exposure	100%

Strategy / Security	Manager	Asset class	Portfolio value	Proportion of portfolio	Yield ¹
Income strategies				73.1%	
Bank deposits	NZ Funds	Cash	\$1,785,986	3.6%	2.5%
Bank bills	NZ Funds	Cash	\$627,663	1.1%	2.7%
Inflation-linked government bonds	NZ Funds	Government bonds	\$11,794,031	20.0%	5.3%
Investment-grade corporate bonds	PIMCO	Corporate bonds	\$5,967,588	10.1%	7.8%
Investment-grade corporate bonds	iShares	Corporate bonds	\$5,852,580	9.9%	8.4%
High-quality government bonds	NZ Funds	Government bonds	\$3,371,139	5.7%	5.8%
Global government bonds	Franklin Templeton	Government bonds	\$3,123,242	5.3%	6.3%
Loans (via Private Loan Trust)	Fidelity	New Zealand direct loans	\$1,527,305	2.0%	7.3%
Share hedge ²	NZ Funds	Cash	\$8,987,612	15.3%	2.5%
Growth strategies				26.9%	
Global property	Challenger/Resolution/NZ Funds	Global property	\$6,094,845	10.4%	4.7%
Global shares - Core	Lazard	Global shares	\$4,199,314	7.1%	5.4%
Global shares - Growth	T Rowe Price	Global shares	\$3,920,509	6.7%	5.2%
Global shares - High dividend yield	Tweedy Browne	Global shares	\$3,734,961	6.3%	6.8%
Global shares - Utilities	NZ Funds	Global shares	\$2,993,835	5.1%	7.1%
Commodities	S&P Goldman Sachs	Commodities	\$2,983,763	5.1%	n/a
Australasian shares - High dividend yield	NZ Funds	Australasian shares	\$906,117	1.5%	7.1%
Share hedge ²	NZ Funds	Global shares	-\$8,987,612	-15.3%	2.5%
Currency strategies					
Foreign currency exposure	NZ Funds	Fully hedged	\$0	0.0%	n/a
Total economic exposure			\$58,882,878	100.0%	5.7%

¹ The yield calculation represents an estimate of the yield on the Portfolio, calculated using the most recent information provided by the investment managers involved in managing the Portfolio, hedged back to New Zealand dollars where appropriate. It is not calculated 'as at' any particular date as different investment managers provide data at varying dates. As a result, in some instances the yields may lag the date of this portfolio summary. The yield is not the return on the Portfolio, nor is it a projection or forecast. Rather, it is an estimate of the pre-tax and fees income stream generated from investing in the Portfolio. The Portfolio return consists of yield and capital gains and losses (also calculated on a pre-tax and fees basis). Therefore, the Portfolio's return could be less than the Portfolio's yield. Details of the yield calculation are available on request from NZ Funds. ² The effect of the share hedge is to reduce the allocation to shares and increase the allocation to cash. Note: Rounding may affect the subtotals and totals.

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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