

APRIL 2010

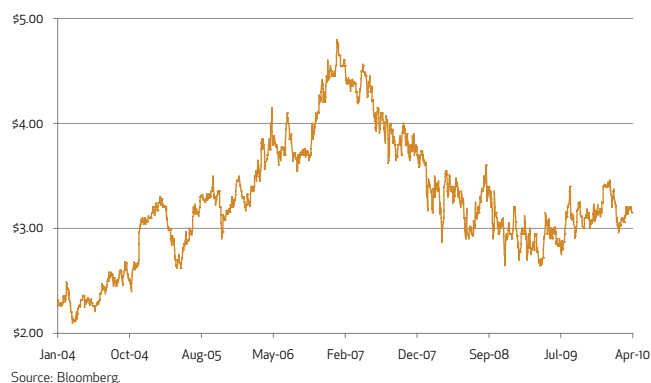
Freightways' performance in the first half of the 2010 financial year is ample proof that at the coal face of services and manufacturing, business has been a struggle. It's a reminder, if any was needed, that the recession we have recently emerged from has been long and difficult. Yet the express package and information management company has dealt with the environment as well as can be expected and remains well positioned to benefit from an economy that is slowly returning to growth.

While Freightways is a business that has demonstrated a strong element of defensiveness as the economy slowed, its performance in the first quarter of 2010 covers a period when the economy was at its weakest. The company's results showed that there was no escape for its core express package division (which accounts for around 80% of revenue and a similar proportion of earnings). In that division the volume of business from existing customers was 5 per cent lower than the previous period. Although the company has a high degree of variable costs (because its owner drivers get paid per parcel they deliver) a volume decline of that amount can't help but affect margin.

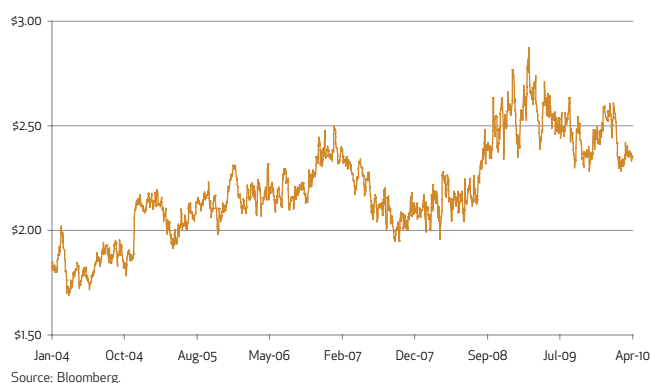
Although its performance has been weaker than expected the overall investment case for Freightways remains sound. As the economy grows so too will physical movement of packages and Freightways will benefit. In fact, this paradoxically confirms their investment case because it emphasises that Freightways remains a cyclical business. It couldn't cut its fixed cost base enough to deal with a 5% volume decline but when volume growth returns those costs won't grow and although the variable costs will, earnings will grow faster than revenue.

Following its latest result, Freightways price fell and is now trading at above \$3. The stock is priced at an enterprise value to EBIT multiple of 11.4x, which is not overly cheap but that figure represents earnings at a cyclical low. When volume growth returns you can expect to see margins widen and earnings rapidly improve. If historic margins are applied to the relatively weak revenues expected for the full 2010 financial year then the stock would earn EBIT of \$64m, an operating earnings yield (or pre-tax return to investors) of more than 10% per annum. This doesn't take into account the very strong record the company has of growing sales. In addition the investors are getting a cash dividend yield of 5 per cent.

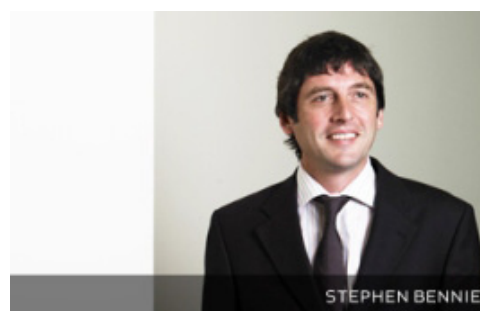
### FREIGHTWAYS PRICE



### FREIGHTWAYS RELATIVE TO NZ SHARES



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