

*"In the business world, the rearview mirror is always clearer than the windshield..."*

Warren Buffet

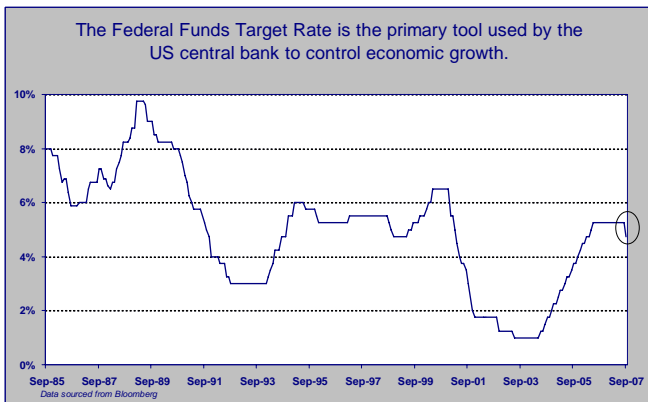
**Global growth to remain stable**

The main theme for the quarter to 30 September 2007 has been an increased awareness of problems in the US housing market. In particular, rising default rates on US sub-prime home mortgages – which are made to borrowers of lesser credit quality – have caused concern.

It was feared that the weaker housing market may lead the economy into a recession. As the US is the world's largest economy, a recession in this country would have an adverse impact on global growth.

The Federal Reserve (Fed), the US central bank, responded in the middle of September by lowering its target interest rate by 0.50% to 4.75% in an attempt to support the economy.

This was the first time the Fed lowered interest rates in the past four years. Furthermore, the Fed has indicated that it will take the necessary steps to ensure that the US doesn't enter a prolonged economic slowdown. This bodes well for global growth.



It should be noted that although the US economy is in many respects the key to global growth, its dominance has become less over time. The economies of countries such as China, India and Russia, as well as many of the Latin American countries, have shown significant growth in recent years.

China, in particular, will play a far more significant role in global growth going forward.

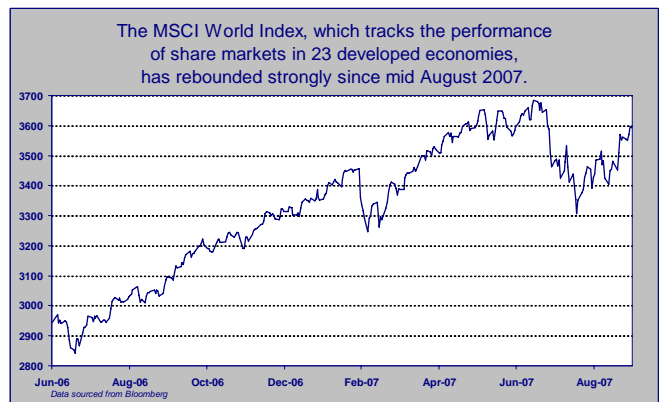
In July, the International Monetary Fund (IMF), an international organisation of 185 countries established to oversee the global financial system, forecast China's economy to grow by 11.2% and 10.5% in 2007 and 2008 respectively. To put this in context, the IMF has forecast the US economy to grow by 2.0% and 2.8% over the same periods.

**Global equities fall and then rebound strongly**

The quarter to 30 September 2007 was a relatively volatile period for international equities. The impact of concerns about sub-prime mortgages in the US was first felt in global credit markets, which then led to a 'knock-on' effect in equity markets.

There was a 'flight to quality' as investors sold riskier assets and placed their money in safer investments. As a result, global equity markets fell sharply from the middle of July to the middle of August. Thereafter, the remainder of the quarter was characterised by a strong rebound in global equities as investor confidence returned.

The MSCI World Index, which tracks equity markets in 23 developed economies, was flat for the quarter in local currency terms. Of the major stock markets, the Nikkei – an index of Japan's top 225 blue-chip companies – was down the most with a return of -7.5%. However, the MSCI Emerging Markets Index – which tracks share markets in 26 emerging economies such as Brazil, China and India – was up 11.8% in local currency terms.

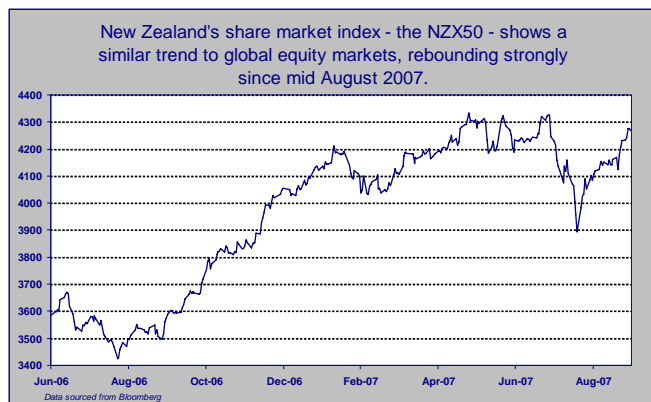


For investors with an unhedged (or partially-hedged) exposure to global equities, the depreciation of the New Zealand dollar

against all major currencies over the quarter will have benefited their returns.

### A similar experience for New Zealand equities

The New Zealand equity market followed much the same course as global equity markets over the quarter. The benchmark NZX50 Index – which tracks the 50 largest local stocks – was relatively flat, with a return of 0.8% for the quarter.



The month of August saw a number of companies report their financial results for the year ending June 2007. In general, companies achieved or exceeded forecasts.

Merger and acquisition activity continues to influence domestic equity prices with companies such as Auckland International Airport becoming subject to a variety of takeover offers.

SkyCity Entertainment, one of the most prominent gaming operators in Australasia, is currently in talks with an unnamed party that has expressed an interest in purchasing 100% of its shares. If this takeover goes ahead, SkyCity Entertainment will join the list of companies such as Carter Holt Harvey and Waste Management that have been de-listed from the New Zealand Stock Exchange.

### High interest rates for some time yet

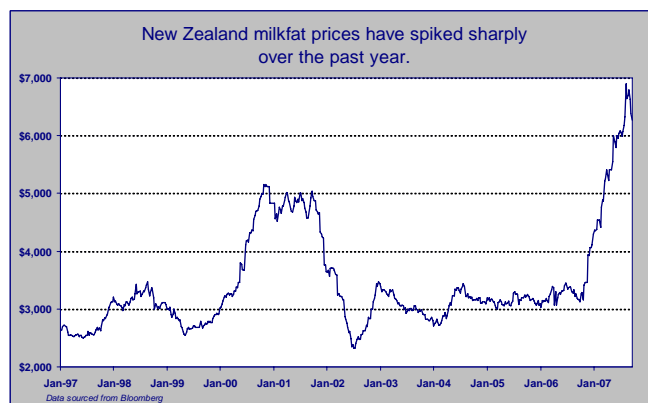
High interest rates have started to have a discernable effect on certain sectors of the economy, with consumers stepping back from the purchase of big-ticket items such as cars and furniture.

The housing market has also softened as the average price of a home in New Zealand increases at a slower rate and the number of homes being sold falls.

A number of inflationary pressures persist in our economy and, therefore, the Reserve Bank could maintain the Official Cash Rate (OCR) at current levels for some time.

The inflationary pressures referred to include higher petrol and food prices, a low unemployment rate, increased government spending and speculation of tax cuts in the run-up to elections next year. Higher milkfat prices have increased payouts to dairy

farmers and will contribute further to these inflationary pressures over time as discretionary spending from this sector increases.



### Positive signs start to emerge from credit markets

Over the past quarter to 30 September 2007, there has been a sea change in the attitudes of investors towards risk in global credit markets.

In late July and August, these markets moved from a position of having excess liquidity – where banks and investors were very willing to lend money – to an environment of excessive caution where banks and investors were unwilling to advance money. This sudden reversal in conditions was initially driven by problems in the US housing market.

Central banks in the US, Europe and Japan then stepped in to provide sufficient liquidity to prevent the global banking system from going into gridlock.

In September, there was a noticeable change in sentiment in global credit markets. This was mainly due to the US Fed lowering its target interest rate. With less risk of the US economy slipping into a recession, investors have been more willing to return to credit markets.

Although there is still an overhang of sellers within these markets, particularly the market for structured credit assets, the volume of new debt issuance by companies improved in September. This compares favourably with the situation in late July and August when new issuance slowed dramatically.

Also worth noting is that there has been an increase in trading within these markets, which has led to greater transparency regarding prices and, therefore, more accuracy in valuing assets.

Looking ahead, returns from credit markets should improve as the imbalance between demand and supply corrects itself over time.

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