**17 October 2013**
**NZX**

**Directors' Report to Shareholders**
**For the 28 Weeks ended 9 September 2013**

**Key Points**

| | 1H 2014 | 1H 2013 | Change ($) | Change (%) |
|---|---|---|---|---|
| **Total Group Revenue ($m)** | **176.0** | **167.2** | **+8.9** | **+5.3** |
| **Group Net Profit after Tax* ($m)** | **8.8** | **8.8** | **-** | **+0.9** |
| **Dividend (cps)** | **6.5** | **6.5** | **-** | **-** |

*Excluding non-trading items*

- Net Profit after Tax (excluding non-trading items) for the 28 weeks ended 9 September 2013 (1H 2014) was $8.8 million (9.0 cents per share), the same as the prior period (1H 2013). Reported profit (including non-trading items) was $9.7 million (9.9 cents per share), up $2.8 million or 41.4% on the prior period.

- Total revenues of $176 million were up 5.3% on the previous half year, mainly because of the contribution from the new Carl's Jr. brand. Same store sales were up 2.9% for the half year, driven by ongoing improvement in Pizza Hut which was up 19.3%.

- Total brand EBITDA was up $0.2 million to $27.2 million, with a very strong performance by Pizza Hut, partly offset by lower earnings from KFC and new store establishment costs in Carl's Jr.

- Non-trading items made a positive pre-tax contribution of $1.1 million, mainly arising from the successful sale and leaseback of two KFC stores in Lower Hutt and Greenlane.

- Directors have declared a fully imputed interim dividend payable on 22 November 2013 of 6.5 cents per ordinary share, consistent with last year.

**Group Operating Results**

Restaurant Brands' unaudited net profit after tax (excluding non-trading items) for the 28 weeks ended 9 September 2013 (1H 2014) was $8.8 million or 9.0 cents per share, in line with prior year (1H 2013). Reported profit was $9.7 million (9.9 cents per share), up 41.4% on prior year due to a positive contribution from non-trading items.

Total operating revenue at $176.0 million was up $8.9 million (or 5.3%) on the prior year, primarily driven by $6.6 million in sales from the new Carl's Jr. brand. Same store sales were also positive at 2.9% because of a very strong performance by Pizza Hut.

Brand EBITDA at $27.2 million was $0.2 million up on prior year. KFC earnings were down by $1.1 million (4.4%), but this was more than offset by a $1.5 million or 88.3% increase in Pizza Hut EBITDA. Starbucks Coffee was in line with prior year. Carl's Jr. had a small loss of $0.2 million as new store opening costs were incurred as expected.

The ongoing challenges in the retail environment have continued to suppress margins, but directors are pleased the company has been able to hold total brand EBITDA slightly above last year's levels.

A profit in non-trading items of $1.1 million, compared with a $2.9 million loss in the previous half year, largely arose from the successful sale and leaseback of two KFC stores.

Store numbers totalled 174 at the end of the half, eight down on prior year. Increases in numbers of KFC and Carl's Jr. stores with new builds were more than offset by Pizza Hut disposals and Starbucks Coffee closures.

**KFC**

| | 1H 2014 | 1H 2013 | Change ($) | Change (%) |
|---|---|---|---|---|
| **Sales ($m)** | **129.3** | **127.4** | **+1.8** | **+1.4** |
| **EBITDA ($m)** | **22.8** | **23.9** | **-1.1** | **-4.4** |
| ***EBITDA as a % of Sales*** | ***17.7*** | ***18.7*** | **-** | **-** |

KFC's total sales were $129.3 million, up 1.4% or $1.8 million on prior year. Same store sales were flat at -0.1%. Strong competition, a soft marketplace and in particular the impact of value campaigns all kept pressure on same store sales growth. Total sales growth was assisted by the new and transformed stores completed in the back half of the previous financial year, including a new store at Silverdale and one acquired from an independent franchisee in Cambridge.

KFC launched a number of successful promotions over the quarter including the return of *Hot 'n Spicy*, a new *Double Down* variant and the *Kentucky Burger*.

Despite continuing operating efficiencies, margins were adversely impacted by the need to introduce a value strategy to meet the market. The $1,2,3 menu range was successful in generating sales, but had an adverse effect on margin with a resultant 4.4% decrease in EBITDA on prior year to $22.8 million (17.7% of sales).

The transformation process was slowed over this half with only one major transformation being completed (Otahuhu), bringing a total of 69 out of 89 KFC stores now new or fully transformed. In addition the brand has begun undertaking several five year upgrades of stores previously transformed.

**Pizza Hut**

| | 1H 2014 | 1H 2013 | Change ($) | Change (%) |
|---|---|---|---|---|
| **Sales ($m)** | **26.6** | **25.9** | **+0.7** | **+2.7** |
| **EBITDA ($m)** | **3.1** | **1.7** | **+1.5** | **+88.3** |
| ***EBITDA as a % of Sales*** | ***11.8*** | ***6.4*** | **-** | **-** |

Pizza Hut continued to deliver strong improvements in sales and margin over the half year on the back of its strong everyday value offers.

Same store sales continued to show strong growth, delivering a 19.3% increase for the half year, rolling over a 19.5% increase in the previous year. Total sales were also up by 2.7% to $26.6 million, despite a 17.5% (11 store) reduction in store numbers with the sell down programme.

Continuing sales leverage and tight operational controls saw Pizza Hut EBITDA increase $1.5 million to $3.1 million for the half year (88.3%). EBITDA margin also improved from 6.4% of sales to 11.8%.

Pizza Hut finished the half with 52 stores, 11 less than the prior year with 31 stores now sold to independents (five in this half year).

The sales of lower volume and regional stores to independent franchisees will continue with further stores expected to be sold by the end of the financial year.

**Starbucks Coffee**

| | 1H 2014 | 1H 2013 | Change ($) | Change (%) |
|---|---|---|---|---|
| **Sales ($m)** | **13.0** | **13.4** | **-0.4** | **-2.9** |
| **EBITDA ($m)** | **1.4** | **1.4** | **-** | **-1.6** |
| ***EBITDA as a % of Sales*** | ***10.9*** | ***10.7*** | **-** | **-** |

Although there was a small reduction in total sales of 2.9% because of having five stores less than the prior year, the Starbucks Coffee brand enjoyed solid same store sales growth of 4.0% for the half year to $13.0 million.

Margins held for the brand resulting in an EBITDA flat to prior year of $1.4 million (10.9% of sales).

Store numbers were 28 at balance date, five down on the prior year with one store (Mt Maunganui) closing during the half.

**Carl's Jr.**

| | 1H 2014 | 1H 2013 | Change ($) | Change (%) |
|---|---|---|---|---|
| **Sales ($m)** | **6.6** | **-** | **+6.6** | **-** |
| **EBITDA ($m)** | **-0.2** | **-** | **-0.2** | **-** |
| ***EBITDA as a % of Sales*** | ***-2.6*** | **-** | **-** | **-** |

The Carl's Jr. brand began to gain momentum with a further three stores opening over the half year in Auckland Central, Frankton and Rotorua to bring total store numbers to five. All stores have opened with very strong initial sales and have settled back to sales volumes at levels slightly higher than KFC.

The brand produced a small EBITDA loss for the half of $0.2 million, reflecting as expected the impact of pre-opening costs such as staff training, together with settling in costs post-opening.

**Corporate & Other**

General and administration (G&A) costs at $7.2 million were flat compared to the prior half year and ran at 4.1% of sales, marginally over the 4.0% target.

Depreciation charges of $7.6 million for the half year were marginally up on the prior year with KFC and Carl's Jr. showing an increase as a result of their transformation and new store capital expenditure and Starbucks Coffee and Pizza Hut showing corresponding reductions with store closures and sales to independent franchisees.

Amortisation charges also rose by $0.2 million, mainly as a result of Carl's Jr. franchise fees and some software development costs.

Funding costs remained flat at $0.4 million with similar interest rates and debt levels.

Tax expense was $1.2 million up on the prior year with higher reported profit levels. The effective tax rate of 26.9% is slightly higher than prior year's 25.9% with higher effective non-deductible items.

**Non-Trading Items**

Non-trading items showed a positive balance of $1.1 million, a significant change on the $2.9 million loss in the previous half year. The sale and leaseback of the KFC stores in Greenlane and Lower Hutt produced a gain on disposal of $1.5 million, with Pizza Hut store divestments producing another $0.1 million gain on book value. The gains were partly offset by write-offs as a result of store closure provisions and KFC transformations.

**Cash Flow & Balance Sheet**

Total assets of $110.9 million were similar to the last year end. Property, plant and equipment was down to $80.4 million versus $85.7 million at year end from Pizza Hut store disposals, but current assets were up to $8.8 million from $4.8 million with higher inventory levels and the Carl's Jr. Frankton site (at $2.5 million) being classified as held for sale.

Total liabilities at $50.1 million were down $1.3 million on the previous year end with total borrowings reduced by $4.6 million to $10.2 million, partly offset by an increase in current liabilities with creditors and accruals increasing by $5.2 million compared to prior year end.

Operating cash flows were $17.0 million, $2.8 million down on the previous half year mainly because of higher tax payments ($1.9 million) and the fact that the prior period had included the receipt of significant business interruption insurance proceeds from the Christchurch earthquake.

Cash outflows from investing activities of $3.0 million were similar overall to the prior half year. Investing payments in this half were $12.2 million (compared with $5.2 million in the prior year), reflecting incremental Carl's Jr. capital expenditure. Investing receipts were also strongly up to $9.2 million (versus $2.1 million in the prior year). This largely arose from final earthquake material damage insurance receipts and the impact of the sale and leaseback of the two KFC stores.

With $14 million in free cash flow for the half year, debt was reduced by $4.6 million reducing total borrowings to $10.2 million.

**Dividend**

Given that the financial performance for the first half is anticipated to continue for the balance of the year, the relatively low levels of debt and measured approach to capital expenditure requirements to bring the Carl's Jr. stores progressively to market, the board has declared an interim dividend of 6.5 cents per share, the same as the prior year.

The interim dividend will be fully imputed and payable on 22 November to all shareholders on the register on 8 November 2013. A supplementary dividend of 1.1471 cents per share will be paid to all overseas shareholders at the same time.

Directors have elected to continue to suspend the dividend reinvestment plan for the time being, but will review this again prior to the declaration of a final dividend.

**Outlook**

Whilst there has been some improvement, trading conditions remain challenging and the QSR market continues to see heavy price discounting. All four brands have continued to build internal efficiencies around current pricing pressures and will be well positioned to benefit from any upside when the market stabilises.

KFC is expected to maintain positive sales growth and, market circumstances permitting, bring some margin improvement in the second half.

Pizza Hut has continued to hold the sales gains made last year and is expected to maintain current margins, while continuing the store sell down programme.

Starbucks Coffee will hold sales and margin.

Carl's Jr. will see a continuation of store roll out with a further three stores scheduled for opening in the second half of the year. The brand is expected to begin returning positive EBITDA margins in the second half.

Directors therefore anticipate an improvement in profit in the second half to a full year NPAT (excluding non-trading items) in the vicinity of $18-19 million.

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**ENDS**

**RESTAURANT BRANDS GROUP**
**Consolidated Income Statement**
**For the 28 week period ended 9 September 2013 (2014 Half Year)**

| $NZ000's | (28 weeks) Unaudited 1st Half 2014 9 September 2013 | | vs Prior % | (28 weeks) Unaudited 1st Half 2013 10 September 2012 | |
|---|---|---|---|---|---|
| **Total operations** | | | | | |
| **Sales** | | | | | |
| KFC | 129,264 | | *1.4* | 127,443 | |
| Pizza Hut | 26,577 | | *2.7* | 25,884 | |
| Starbucks Coffee | 12,975 | | *(2.9)* | 13,369 | |
| Carl's Jr. | 6,628 | | *n/a* | - | |
| **Total sales** | **175,444** | | *5.2* | **166,696** | |
| Other revenue | 576 | | *23.9* | 465 | |
| **Total operating revenue** | **176,020** | | *5.3* | **167,161** | |
| Cost of goods sold | (147,199) | | *(6.7)* | (137,905) | |
| **Gross margin** | **28,821** | | *(1.5)* | **29,256** | |
| Distribution expenses | (1,407) | | *8.0* | (1,529) | |
| Marketing expenses | (7,676) | | *3.1* | (7,921) | |
| General and administration expenses | (7,205) | | - | (7,204) | |
| **EBIT before non-trading** | **12,533** | | *(0.5)* | **12,602** | |
| Non-trading | 1,130 | | *138.6* | (2,924) | |
| **EBIT** | **13,663** | | *41.2* | **9,678** | |
| Net financing expenses | (396) | | *8.3* | (432) | |
| **Net profit before tax** | **13,267** | | *43.5* | **9,246** | |
| Taxation expense | (3,573) | | *(49.6)* | (2,388) | |
| **Total profit after tax (NPAT)** | **9,694** | | *41.4* | **6,858** | |
| **Total NPAT excluding non-trading** | **8,837** | | *0.9* | **8,762** | |
| | | **% sales** | | | **% sales** |
| **EBITDA before G&A** | | | | | |
| KFC | 22,826 | *17.7* | *(4.4)* | 23,877 | *18.7* |
| Pizza Hut | 3,129 | *11.8* | *88.3* | 1,662 | *6.4* |
| Starbucks Coffee | 1,410 | *10.9* | *(1.6)* | 1,433 | *10.7* |
| Carl's Jr. | (170) | *(2.6)* | *n/a* | - | *n/a* |
| **Total** | **27,195** | ***15.5*** | ***0.8*** | **26,972** | ***16.2*** |

| | | |
|---|---|---|
| **Ratios** | | |
| Net tangible assets per security (net tangible assets divided by number of shares) in cents | 43.3c | 40.0c |

Cost of goods sold are direct costs of operating stores: food, paper, freight, labour and store overheads.
Distribution expenses are costs of distributing product from store.
Marketing expenses are call centre, advertising and local store marketing expenses.
General and administration expenses (G&A) are non-store related overheads.