10 April 2008

RESTAURANT BRANDS NEW ZEALAND LIMITED

Directors' Report to Shareholders for the Year ended 29 February 2008

Key Points

- Total sales for the company were $303.5 million, up $9.9 million on prior year with same store sales up 3.4%.

- Record sales for KFC at $199.1 million (up 7.7% on a same store basis) and Starbucks Coffee ($33.0 million, up 4.0% on a same store basis) were partly offset by lower sales of $71.4 million for Pizza Hut, down 7.0% on a same store basis.

- Group Net Profit after Tax (excluding non trading items) was $11.0 million, up $4.5 million or 69% on prior year, mainly because of the strong result for KFC and the cessation of losses in Pizza Hut Victoria.

- Sale of the Pizza Hut Victoria business was finalised with all residual stores bar one disposed of or closed. The disposal of the remaining store will be completed by month end.

- The KFC brand transformation continued its roll out with significant sales growth in the 30 transformed or new stores.

- Strong operating cash flows (up $10.5 million on 2006/7) saw debt reduce by $6.1 million on prior year, notwithstanding the continuing significant investment in KFC transformation.

- A final full year fully imputed dividend of 3.5 cents per share has been declared making a full year dividend of 6.5 cents, up 1 cent on prior year.

Group Operating Results

The 2007/8 year has been one of solid improvement over last year driven by a very strong performance by the KFC business.

Net Profit after Tax excluding non trading items was $11.0 million compared to $6.5 million for the prior year. The improvement was due to New Zealand operations profit up $1.4 million with $3.1 million from cessation of losses in Pizza Hut Victoria. Reported NPAT (including non-trading items) was $9.0 million, compared with a loss of $3.6 million in the 2006/7 year.

Non-trading charges of $3.4 million mainly comprised $0.8 million in fixed asset write offs under the KFC transformation programme, $0.9 million in Pizza Hut New Zealand store closures (largely red roofs) and a further $1.2 million in Pizza Hut goodwill impairment charges following a review of the carrying value of this investment. A further $0.5 million (net of tax) was taken up against the Victoria exit provision, representing the continued delays over the year in finally achieving an exit from this business.

Total sales of $303.5 million were up $9.9 million or 3.4% on prior year sales. Same store sales for the group were up 3.4%. Both KFC and Starbucks Coffee demonstrated continuing solid sales growth, up 7.7% and 4.0% respectively on a same store basis, but Pizza Hut New Zealand saw same store sales drop 7.0% for the year.

Store EBITDA for the year was up $5.2 million to $45.1 million. Almost all of this growth was from KFC.

Above store overheads (G&A costs) at $11.0 million were down $0.1 million on prior year and are running at 3.6% of sales compared with 3.8% in 2006/7.

Depreciation charges were up $1.7 million on prior year with most of the increase being as a result of KFC transformation capex.

Year end store numbers at 228 in New Zealand were 9 down on February 2007 following 6 Pizza Hut store closures (mostly as part of the red roof exit strategy). In addition a net three Starbucks Coffee stores were closed.

As at the date of this announcement all remaining stores in Victoria bar one had been sold or closed and it is expected the final transaction will be completed by month end.

KFC
KFC enjoyed yet another year of sound sales and profit growth driven by the continued transformation campaign. Total sales reached a new record of $199.1 million, up $16.4 million or 9.0% on prior year (7.7% same store).

A further 9 stores were transformed over the year bringing total transformed and store numbers to 30, over 1/3 of the total network. Store numbers remained constant at 87.

Earnings were also up strongly, with EBITDA improving by $5.4 million (17.3%) to $36.6 million (18.4% of sales). Continuing excellent operational controls and the benefit of volume leverage from increased sales were the main drivers of this record profit performance.

Pizza Hut New Zealand
The Pizza Hut New Zealand business continued to face tough trading conditions with slow progress in restoring sales growth and profitability. Sales of $71.4 million for the year were down 7.0% on a same store basis.

The impact of the drop in sales, together with some cost increases, particularly in labour, saw further margin deterioration with the brand producing an EBITDA result of $4.7 million for the year, $0.4 million down on prior year. It is of note however, that the bulk of the shortfall versus prior year occurred in the first half with subsequent trading producing a $0.4 million improvement in EBITDA, despite the continuing sales shortfalls.

The new operational and marketing initiatives introduced over the past 12 months now mean that the business is capable of producing a profit even at the current lower sales volumes.

As part of the initiatives to restore profitability, a number of stores closed over the course of the year. Five red roof restaurants at Northcote, Palmerston North, Papakura, Dunedin and Queenstown were closed as part of a wider exit strategy and one delco at Eastridge in Auckland closed at lease end. This brought store numbers at year end to 97.

Starbucks Coffee
Sales growth of 5.6% (4.0% same store) saw Starbucks Coffee revenues exceed $33.0 million for the first time.

The sales growth is pleasing, given a reduction in store numbers of three over the year to 44 at year end. This store rationalisation involved the closure of four stores; two non performing stores at 105 Queen Street and Lynnmall (both in Auckland), the flagship Downtown Auckland store (because of site redevelopment) and the Albany store at lease end. One new store in Victoria Street, Auckland was opened during the year.

The continuing impact of higher labour costs was largely offset by lower material costs and the leverage effect of higher sales to produce an EBITDA of $3.9 million, up $0.2 million on prior year.

Cash Flow and Balance Sheet
The strong trading result for the KFC operations and the reduction in cash losses from the Victoria Pizza Hut business resulted in operating cash flows improving to $31.3 million, up $10.5 million on prior year.

Investing cash flows of $18.5 million were $11.1 million down on prior year. The capex levels in 2006/7 were particularly high with transformation spend at its peak, new store builds across all three brands and the purchase of new computer systems. Expenditure on KFC transformation in the current year was $10.5 million and franchise renewals comprised another $3.3 million.

The improved cash position has meant that borrowing levels have reduced by $6.1 million over the year with closing bank debt of $42.5 million, well within current facility limits of $70 million.

Total assets at $113.0 million were down on the $117.7 million at last year end.

Franchise Renewals
The company renewed the 47 of its KFC franchises over the year and continued to secure 10+10 year franchises on its transformed stores. Eight Pizza Hut franchises were also renewed.

Board and Management
Russel Creedy was appointed as CEO in September 2007, following the boards' extensive international search process. Mr Creedy's appointment followed six months in an acting role following the resignation of Vicki Salmon.

There were no changes in directorships over the year.

Dividend
With the improving financial performance of the company the board has elected to increase the final dividend to 3.5 cents per share. This brings the total dividend for the year to 6.5 cents from 5.5 cents last year.

The dividend will be paid on 27 June 2008 to all shareholders on the register as at 13 June 2008. A supplementary dividend of 0.61765 cents per share will also be paid to overseas shareholders on that date.

With the change in corporate tax rate for the new financial year, 1.65 cents per share of the dividend will be paid as imputed at 33% and the balance at 30%, giving a weighted average imputation credit of 1.60555 cents per share.

The dividend reinvestment plan will remain suspended for this dividend.

Outlook
Whilst this year's trading results represent a significant improvement over prior year's performance, directors remain cautiously optimistic as to future outlook.

Investment in the KFC transformation programme will continue and this business is expected to continue to deliver sales growth.

The Pizza Hut New Zealand profit recovery is anticipated to continue although total sales growth is not expected to be positive due to continuing store rationalisation, particularly of the red roof stores.

Starbucks Coffee is forecast to continue steady sales growth and a margin improvement on prior year.

The 2007/8 year has been one of rebuilding for the company. With the Pizza Hut Victoria exit finally completed, a higher level of management focus will be made on the Pizza Hut NZ business, with improved results. This, combined with the KFC and Starbucks Coffee sales momentum, is expected to produce a further steady improvement in the 2008/9 profit performance, economic conditions permitting.

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