Devon
FUNDS MANAGEMENT

MONTHLY REPORT

Keeping you up to date with Devon Funds and the markets — June 2016

MARKET COMMENTARY

June 2016 Markets Commentary

What an extraordinary month! The unexpected happened when the United Kingdom voted to leave the European Union. That was followed by an almost unprecedented political collapse inside both the UK Conservative and Labour parties. The UK may break up as there is now uncertainty over the future of Scotland and Northern Ireland within Great Britain. Across Europe, anti-EU parties are gaining support and further referendums are now more likely. And yet, at the time of writing, global equity markets have broadly regained any lost ground and some are even up on their pre-Brexit levels. Common wisdom was that the fall out from Brexit would be severe. So why hasn't that happened?

The short explanation is interest rates. Interest rates globally are at historical lows with an unprecedented 20% of sovereign (government issued) bonds trading at negative interest rates. Against this backdrop global investors are finding it very hard to sell equities as there simply isn't anywhere else to put their money.

The Governor of the Bank of England, Mark Carney, has just signalled that the British central bank will cut interest rates to support the economy and any rate rises from the US Federal Reserve are now likely to be on hold until next year.

Apart from the short-term economic impact, the vote to leave the European Union is fascinating from an historical perspective as it reflects the first significant pushback in recent times by a nation against the globalisation trend.

There has been a surge in support in Europe for anti-EU parties, particularly on the right wing, and this increase in popularity is likely to grow following the UK referendum and perceived ongoing immigration issues. A number of the critical European countries, including Germany and France, have general elections next year and the future of the EU is most likely to be the major issue… Read More

MARKET INDICES

Index	Region	Monthly Return	1 Yr. Return
S&P NZX50 Gross	NZ	-2.0%	20.4%
S&P ASX200	AUSTRALIA	-2.5%	0.6%
MSCI World Index	GLOBAL	-1.1%	-2.2%
S&P500	USA	0.3%	4.0%
FTSE100	UK	4.7%	3.8%
NIKKEI 225	JP	-9.5%	-21.6%
NZ 90 Day Bank Bill	NZ	0.2%	2.9%

AT A GLANCE

UNIT PRICES

DEVON ALPHA FUND	$1.5649
DEVON AUSTRALIAN FUND	$1.2609
DEVON DIVIDEND YIELD FUND	$1.8438
DEVON DIVERSIFIED INCOME FUND	$1.5460
DEVON TRANS-TASMAN FUND	$3.4259
GLOBAL THEMES FUND	$2.0630

Prices as at 30 June 2016

IN THIS REPORT

Level 10, Rabobank Tower, 2 Commerce Street, Auckland 1010
PO Box 105609, Auckland 1143, New Zealand
Phone: 0800 944 049 | +64 9 925 3990 | Fax: +64 9 307 7088
Client Services: admin@devonfunds.co.nz Website: DevonFunds.co.nz

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DEVON ALPHA FUND

FUND OUTLINE

The Alpha Fund invests in a concentrated portfolio of approximately 10 to 15 select companies predominantly listed on the NZ and Australian share markets.

The Fund does not follow any index, is actively managed and aims to generate capital growth over the long term. Currency exposure is actively managed.

DEVON ALPHA FUND

The Alpha strategy was conservatively positioned going into the Brexit vote holding almost 40% of the Fund's value in cash. Although global equity markets have shown resilience subsequent to the UK Referendum, we anticipate volatility will increase over the next 6-months providing us with opportunities to deploy this cash into more attractively priced opportunities.

There were a number of changes made to the portfolio recently including the purchase of shares in Spark Infrastructure, GTN Limited and Resmed. GTN is a major supplier of traffic information to radio and television stations across Australia and has significant growth opportunities to expand their presence across Brazil, Canada and the US over the next few years. Resmed was purchased because the stock currently looks cheap relative to our assessment of fair value and it has the opportunity of achieving margin improvement through the upcoming release of a new range of masks.

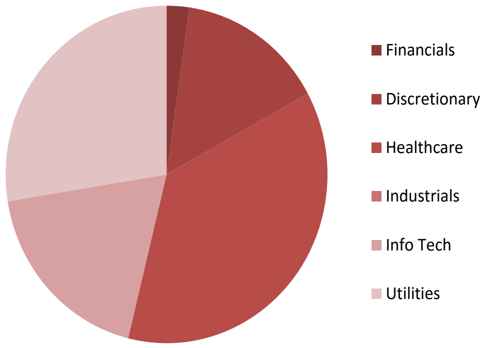
KEY HOLDINGS

sparkinfrastructure

GTN

RESMED

ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

New Zealand Equities	28.2%
Australian Equities	29.6%
Cash	42.2%
	100.0%
Currency Hedge	29.1%

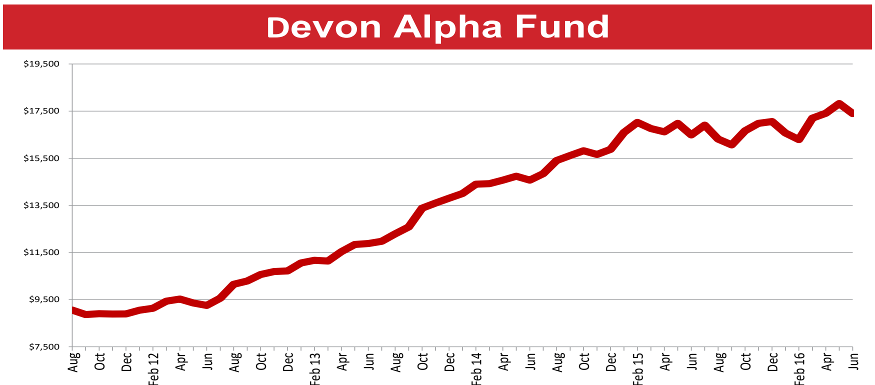
PERFORMANCE

As at 30/06/16	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Alpha Fund	-2.4%	1.1%	5.5%	13.6%	12.7%
OCR	0.2%	0.6%	2.6%	2.9%	2.7%

Devon Alpha Fund returns are after all fees and expenses, but before tax which varies by investor.

NET PERFORMANCE

Based on $10,000 invested at 1 January 2011



PORTFOLIO MANAGER

Slade Robertson

Slade has a long and successful career in investment management. With over 20 years experience in both the New Zealand and Australian investment industries, Slade's excellent track record is proof of his determination to pursue the best investment opportunites for his clients.

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DEVON AUSTRALIAN FUND

FUND OUTLINE

The Australian Fund is actively managed and invests in a select portfolio of approximately 25 to 35 companies which are primarily Australian listed companies.

The Australian market is much larger than the NZ market and offers exposure to a number of sectors that are not available in NZ. The Australian dollar currency exposure of this Fund is typically unhedged.

DEVON AUSTRALIAN FUND

The Australian Fund outperformed the S&P/ASX200 in June amid heightened volatility as Britain voted to exit the European Union. Positive contributors over the month included Resmed, Spark Infrastructure and Stockland. Key detractors were AMP and National Australia Bank.

In terms of portfolio changes, the Fund exited a position in Clydesdale ahead of the UK referendum result. The ASX listed company, which demerged from National Australia Bank earlier this year, was up over 50% YTD and despite a solid cost out story was expensive compared to peers. The Fund also added a position in Crown (CWN). CWN operates two of Australia's largest casinos in Crown Melbourne and Crown Perth along with a stake in Macau's Melco Crown. CWN announced it will be demerging its international assets, look at an IPO of a 49% interest in a property trust that would own Crown Resorts' Australian hotels and adopt a new dividend policy for the core casinos business to pay 100% of NPAT. We made 4 visits to Australia in recent months meeting with over 60 Australian companies and continue to find exciting ideas for the portfolio.

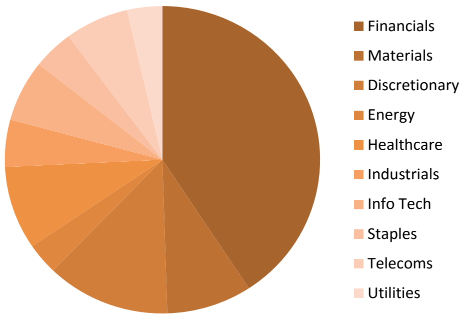
KEY HOLDINGS

ResMed

GTN

Suncorp Group

ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

Dual Listed	6.2%
Australian Equities	89.1%
Cash	4.7%
	100.0%
Currency Hedge	0.0%

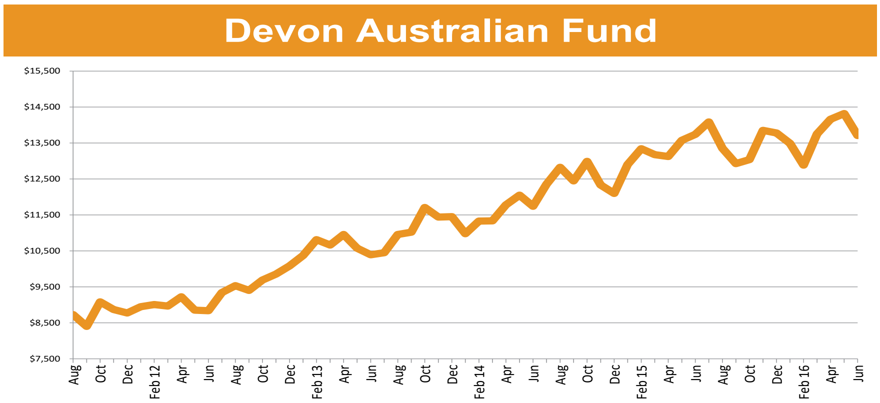
PERFORMANCE

As at 30/06/16	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Australian Fund	-4.3%	-0.3%	-0.2%	9.7%	7.2%
ASX200 Index Gross (NZD)	-4.8%	-1.9%	-7.5%	3.3%	2.9%

Devon Australian Fund returns are after all fees and expenses, but before tax which varies by investor.

NET PERFORMANCE

Based on $10,000 invested at 1 January 2011



PORTFOLIO MANAGER

Tama Willis

A 14-year veteran of international investment markets, Tama returned to NZ after a very successful career in London and Singapore to join Devon's investment team and holds responsibility for Devon's Australian and Trans Tasman Funds. Tama is widely regarded as a leading expert on resource and mining stocks.

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DEVON DIVERSIFIED INCOME FUND

FUND OUTLINE

The Devon Diversified Income Fund aims to give New Zealanders access to a diverse and good quality portfolio of high yielding investments.

The Fund aims to generate better-than-bank income rates by investing in a carefully selected portfolio of government and corporate bonds, cash, listed property, infrastructure, utility companies, high yielding equities, credit securities and other yielding financial assets.

DEVON DIVERSIFIED INCOME FUND

The effects of Brexit were felt quickly across the global fixed interest market. US Treasury prices for example soared on the day of the Referendum, leading yields to post their largest single-day drop since November 2011. At one stage the US 10-year yield traded down towards 1.43% as investors went in search for safety but by month-end, this important reference price had risen back above 1.50%. Investors now do not expect any hike by the Federal Reserve in 2016 and this has had implications for the RBNZ.

Recent market pricing suggests that there is a reasonably high chance that they will now cut the OCR at one of their next meetings despite the ongoing strength in local housing. Another possible effect of the recent volatility is the risk that we see New Zealand corporate credit spreads expand to higher levels over the medium-term.

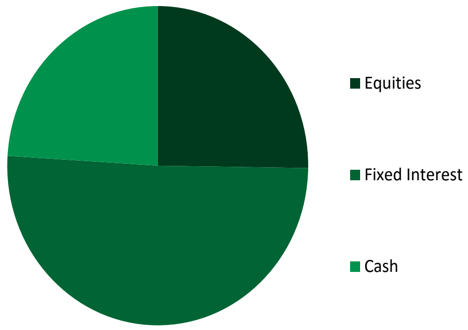
KEY HOLDINGS

Quayside Holdings Ltd

Rabobank

ASB

ASSET ALLOCATION



GROWTH

NZ Equities	12.6%
AU Equities	11.5%

DEFENSIVE

Cash	25.2%
NZ Corporate Bonds	50.7%
NZ Government Bonds	0.0%

PERFORMANCE

As at 30/06/16	1 Mth	3 Mth	Inception
Diversified Income Fund	-0.3%	1.0%	2.8%
OCR +1.5%	0.3%	0.9%	0.74%

Devon Diversified Income Fund returns are after all fees and expenses, but before tax which varies by investor.
Inception date for the Fund is 1 January 2016.

PORTFOLIO MANAGER

Slade Robertson

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AT A GLANCE

Targeted Portfolio Yield	5.5%
Commenced	January 2016
Total strategy	$3.6m
Distributions	Target distributions of 1.5 cents per unit after tax paid quarterly

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DEVON DIVIDEND YIELD FUND

FUND OUTLINE

The Devon Dividend Yield Fund consists of a select group of up to 25-35 New Zealand and Australian listed companies.
These stocks are chosen for their attractive dividend yields and growth prospects with the aim of maintaining the dividend yield and capital value in real terms. The Australian dollar currency exposure is typically fully hedged.

DEVON DIVIDEND YIELD FUND

In a month that saw some large swings as a result of the UK referendum decision to the leave the European Union, the Dividend Yield Fund was not immune to the overall weakness, declining -1.87%. Pleasingly some of the more defensive positions in the portfolio performed in line with expectations, offering a buffer against a weak market.

The standout was Spark Infrastructure Group (SKI), which rose 6.01%. The company was added to the portfolio during May because it offered an attractive headline dividend yield (around 6%), has extremely defensive earnings (it is essentially an investment fund that owns 49% stakes in 3 electricity distribution businesses across Victoria and South Australia), and it has recently completed its major regulatory re-sets and has 5 years before the next round. It also seemed very likely to raise its dividend forecast when the final regulatory draft for Victoria was released – which duly occurred in early June, when the current year dividend and forecast dividends were raised by between 16% and 17%.

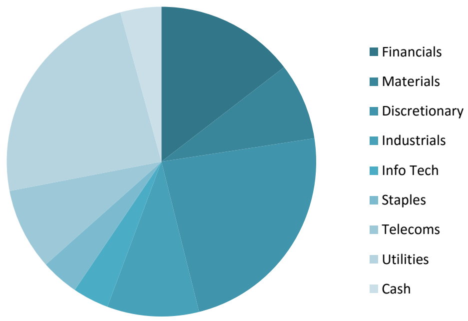
KEY HOLDINGS

Stockland

trademe
Where Kiwis Buy and Sell

sparkinfrastructure

ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

New Zealand Equities	50.0%
Australian Equities	45.7%
Cash	4.3%
	100.0%
Currency Hedge	98.2%
Yield	6.2%

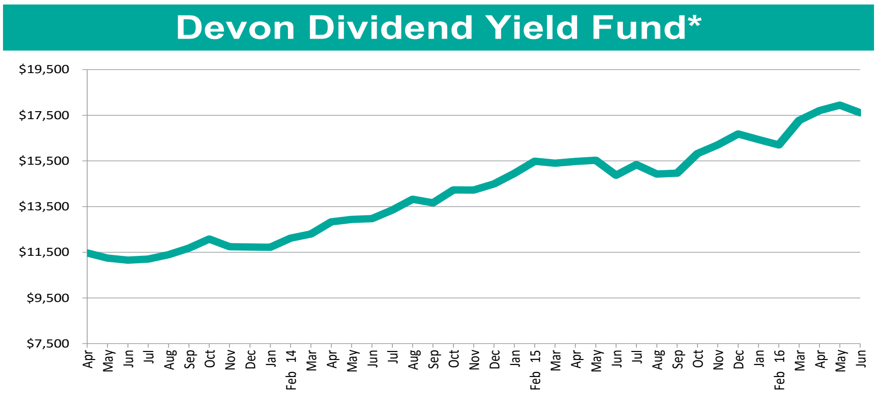
PERFORMANCE

PERFORMANCE As at 30/06/16	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Dividend Yield Fund	-1.9%	1.9%	18.4%	16.9%	-
TT Index (Hedged)	-2.2%	3.0%	10.5%	11.7%	-

Devon Dividend Yield Fund returns are after all fees and expenses, but before tax which varies by investor.

NET PERFORMANCE

Based on $10,000 invested at 20 December 2012



*Fund commenced on 20 December 2012

PORTFOLIO MANAGER

Nick Dravitzki

Over the last decade Nick has specialised in investing in high yield equities and is Portfolio manager for the Devon Equity Income Fund. At Devon, Nick has responsibility for the analysis of consumer staples, IT, consumer discretionary and property sectors. Nick is also responsible for our quantitative screening process.

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DEVON TRANS-TASMAN FUND

FUND OUTLINE

The Trans-Tasman Fund provides a broad and actively managed exposure to the NZ and Australian equity markets.
This Fund typically holds 25 to 35 shares listed on the NZ and Australian stock exchanges which have been carefully selected as offering good value and attractive medium term growth prospects. The Australian dollar currency exposure is typically unhedged.

DEVON TRANS-TASMAN FUND

The Trans-Tasman Fund slightly underperformed the Trans-Tasman index over the month. A positive contributor to Fund performance over the month was Resmed (RMD). RMD is a global healthcare company focused on medical products like masks and flow-generators for the treatment of respiratory disorders and is a key competitor to Fisher and Paykel Healthcare (FPH). RMD currently has 50% of the US flow generator market and is planning to launch a new mask soon which will bolster its competitive offering. RMD trades at a large valuation discount to FPH.

A detractor from performance over the month was SkyCity Entertainment (SKC) as the market digested the departure of CEO Nigel Morrison and a rights issue to reduce balance sheet debt ahead of spending on the Auckland Convention Centre, Hobson Street Hotel and Adelaide casino expansion. The Fund participated in the rights issue and added to the SKC position as the share price fell. In terms of other portfolio changes the Fund exited a position in Clydesdale and Link Administration Holdings ahead of the UK referendum result. Both were strong performers and reached our internal valuations.

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Tama Willis

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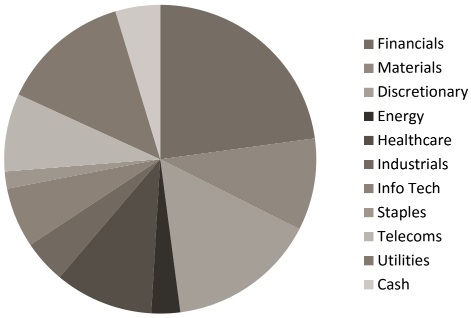
KEY HOLDINGS

oh!media

VISTA GROUP

Contact

ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

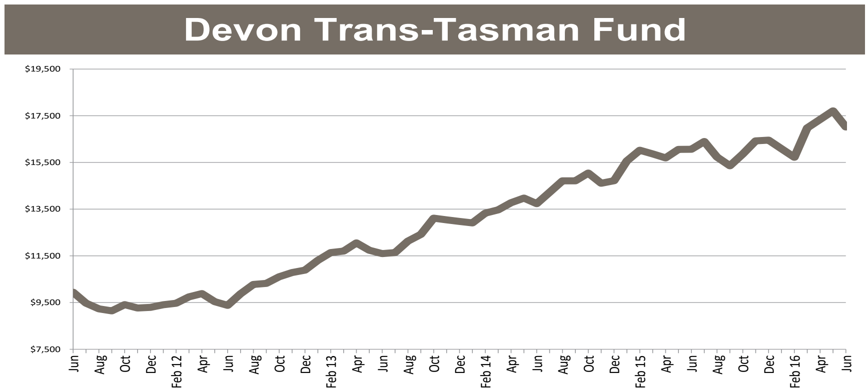
New Zealand Equities	48.9%
Australian Equities	46.5%
Cash	4.6%
	100.0%
Currency Hedge	0.0%

PERFORMANCE As at 30/06/16	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Trans-Tasman Fund	-3.9%	0.2%	5.9%	13.6%	11.3%
Trans-Tasman Index Gross	-3.4%	0.1%	6.5%	9.5%	8.9%

Devon Trans Tasman Fund returns are after all fees and expenses, but before tax which varies by investor.

NET PERFORMANCE

Based on $10,000 invested at 1 January 2011



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GLOBAL THEMES FUND

FUND OUTLINE

The Global Themes Fund invests in Global Financial Assets predominently Global Exchange Traded Funds (ETF's). We identify macroeconomic or thematic investment ideas with a 2-5 year time horizon, and implement the investment ideas through an appropriate high quality assets. Portfolio risk is managed by ensuring broad diversification, ample liquidity and close monitoring of tracking variation versus a passive equity benchmark. The Global Themes strategy has been run by JBWere since March 2005. In October 2014 Devon Funds Management created a NZ PIE Fund to follow the Global Themes strategy and has appointed JBWere as the adviser.

FUND UPDATE

June was an extraordinary month for markets with the Brexit referendum delivering a surprise "Leave" result. This led to a sharp rally in interest rates, a slide in the pound, and violent move across many markets in a short period of time.

Returns were negatively impacted by the Brexit result. Our direct UK exposure was not large, at 5%, but a number of our favourite long term ideas (US Banks, hedged Japan and Europe) were caught in the powerful risk-off episode that ensued. Even as markets recovered through the last days of June, key variables such as 10 year bond yields and the Japanese Yen remain at stretched levels.

In the Fund, we have reduced our European holdings and exited the UK. We think the equity impact of the Brexit result will be more than a two-day wonder for markets, and thus want to lower our exposure to the region. We have lowered our US Banks exposure, but are looking for opportunities to rebuild this provided US economic data remains intact.

More than ever, global equities are embedded with a view that interest rates remain low indefinitely. Futures pricing imply no Fed rate hikes until 2018. We hold the opposite view, which has been the primary driver of our underperformance this year. This polarity of pricing reminds us of similar extreme market episodes in recent history (the tech bubble and the GFC).

Returns

The Global Themes Fund fell 8.8% in June to a unit price of $2.063. This compares with a 2.6% decline in our global equity benchmark. The Fund has risen 3.4% since inception in October 2014, versus a 9.3% increase in the I-Share All Country Exchange Traded Fund 50% hedged to NZD.

Currency exposures

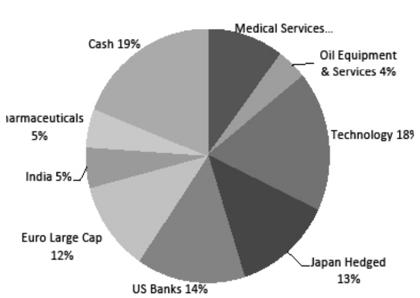
Following the Brexit result we removed almost all of our currency hedging at a little under 70 cents to help de-risk our portfolio. The rebound in the currency since has been a ~2% drag on returns. We remain comfortable being unhedged for now, but are mindful that the NZD is only modestly overvalued. Accordingly we will likely seek to rebuild hedging as opportunities arise.

SENIOR INVESTMENT ADVISER

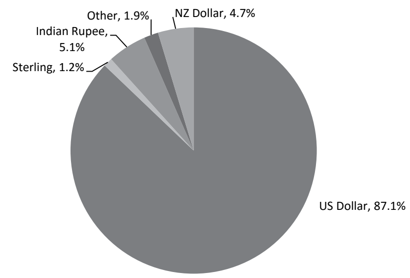
Bernard Doyle

Bernard oversees equity strategy and global tactical asset allocation for JBWere New Zealand. Prior to this role, Bernard was the New Zealand Equity Strategist for Goldman Sachs and Partners, where his team was rated #1 for Strategy and Economics by INFINZ for a number of years. Bernard has 18 years experience in financial markets. He graduated in 1993 with Honours in Economics from Victoria University of Wellington.

SECTOR ALLOCATION

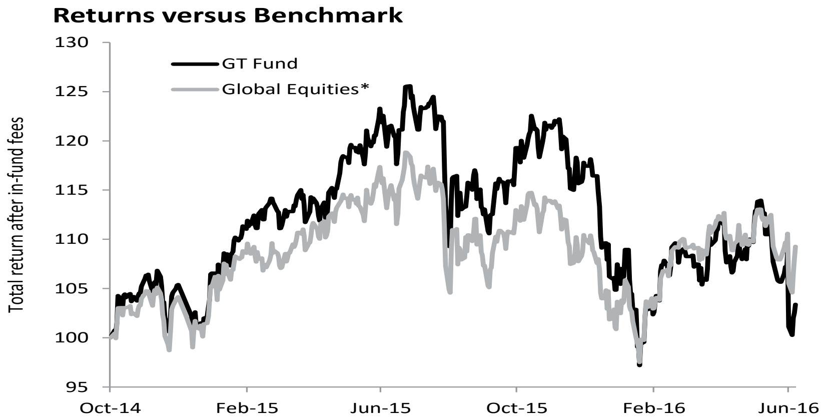


CURRENCY EXPOSURE



NET PERFORMANCE SINCE INCEPTION

Returns versus Benchmark



* iShares MSCI All Country World Index ETF, 50% hedged to NZD
Source: Datastream, IRESS, JBWere Investment Strategy Group

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