

### MARKET COMMENTARY

## It was Rocktober for the NZX

October saw the New Zealand equity market fall -5.4%, its sharpest monthly fall in several years. Since its all-time high, reached on 7 September 2016, the market has declined (at the date of writing) by -11.4%. It has also been notable that the New Zealand market has recently performed much worse than most of its international peers. So, what could be driving the recent activity, and should we be worried (or at least more worried than normal)?

Let's start by putting recent performance in context. As the table below shows, over all but the most recent period, the New Zealand market has been an excellent performer, bettered over 3 years only by the Shanghai index which in that time has been through one of the most extraordinary bubbles (and partial deflations) in history. As the one year performance numbers show, the real outlier has been the New Zealand's market strong rise in the earlier part of the year, which has now partially reversed. Note that these numbers show the S&P/NZX50G and the S&P/ASX200G excluding dividends to make comparison with offshore indices like for like - actual returns to investors in local markets are materially higher both absolutely and relatively due to the high level of dividends paid in Australasia.

Although performance over recent periods has been strong, the sell-off has unquestionably been sharp. When speculating on the potential causes we need to be careful, because we can never know with certainty the cause of short term market movements, but there are some facts that are likely to be relevant. Firstly, the market has looked expensive (when share prices are compared to company earnings) for some time - at its recent peak the market price to earnings multiple rose above 20x, more than 20% above its historic average. Secondly, there has been a marked increase in global bond yields, partly driven by a view that the US Federal Reserve will increase interest rates before Christmas. Finally, we know that there has been a lot of offshore participation in the market in recent years with foreign ownership of the S&P/NZX50G now around 50%, up from around 25% three years ago. With a change in global interest rate views it is likely that some offshore owners will be taking their profits from the NZ market.

Notably there hasn't been a sudden macro-economic shock which has affected the outlook for the performance of...[Read More](#)

### MARKET INDICES

| Index            | Region    | Monthly Return | 1 Yr. Return |
|------------------|-----------|----------------|--------------|
| S&P/NZX50G       | NZ        | -5.4%          | 16.3%        |
| S&P/ASX200G      | AUSTRALIA | -2.1%          | 6.1%         |
| MSCI World Index | GLOBAL    | -1.9%          | 1.8%         |
| S&P500           | USA       | -1.8%          | 4.5%         |
| FTSE100          | UK        | 1.0%           | 13.7%        |
| NIKKEI 225       | JP        | 5.9%           | -6.9%        |



### AT A GLANCE

#### UNIT PRICES

##### DEVON ALPHA FUND

**\$1.5599**

##### DEVON AUSTRALIAN FUND

**\$1.3214**

##### DEVON DIVIDEND YIELD FUND

**\$1.8838**

##### DEVON DIVERSIFIED INCOME FUND

**\$1.5403**

##### DEVON TRANS-TASMAN FUND

**\$3.5222**

##### GLOBAL THEMES FUND

**\$2.2036**

Prices as at 31 October 2016

### IN THIS REPORT

|                         |        |
|-------------------------|--------|
| Market Commentary       | Page 1 |
| At a Glance             | Page 1 |
| Devon Fund Summaries    |        |
| Alpha Fund              | Page 2 |
| Australian Fund         | Page 3 |
| Diversified Income Fund | Page 4 |
| Dividend Yield Fund     | Page 5 |
| Trans-Tasman Fund       | Page 6 |
| Global Themes Fund      | Page 7 |



### 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

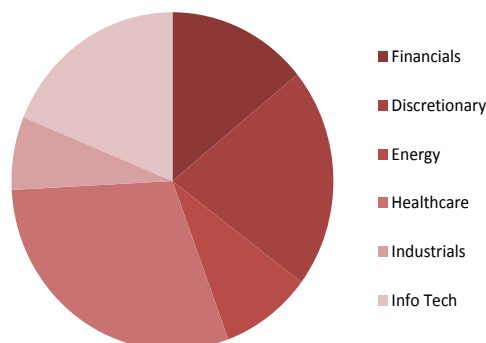
Global equity markets around the world were volatile during October with investors becoming concerned over valuations and the implications of a steepening yield curve. The Alpha strategy was positioned in anticipation of this by maintaining a cash weighting of almost 40%. This served to protect value within the portfolio but unfortunately it was unable to fully mitigate the negative performance of a couple of our Australian investments. Included in this group was Healthscope, the second largest private hospital group in Australia, who saw its share price fall heavily after announcing at their AGM that recent operating performance had been weaker than expected.

We were disappointed with this update but remain positive on the long-term fundamentals of this business and its growth potential from brownfield developments. Offsetting some of the impact of Healthscope was our investment in GTN whose share price rallied strongly after investor confidence increased surrounding their US opportunity.

### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

|                      |        |
|----------------------|--------|
| New Zealand Equities | 28.0%  |
| Australian Equities  | 35.3%  |
| Cash                 | 36.7%  |
| Currency Hedge       | 100.0% |
|                      | 28.3%  |

### PERFORMANCE

As at 31/10/16

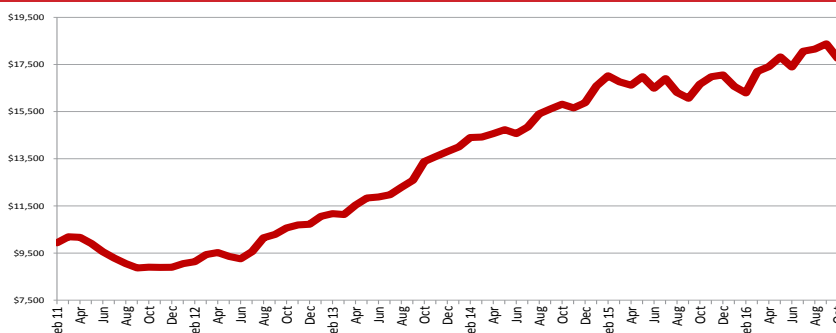
|                  | 1 Mth | 3 Mth | 1 Yr | 3 Yr p.a | 5 Yr p.a |
|------------------|-------|-------|------|----------|----------|
| Devon Alpha Fund | -3.3% | -2.6% | 5.6% | 9.6%     | 14.6%    |
| OCR              | 0.2%  | 0.5%  | 2.3% | 2.9%     | 2.7%     |

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

### Devon Alpha Fund



### 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 opportunities for his clients.



### 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 fell 0.9% over the month, outperforming the S&P/ASX200 in NZD (-1.1%). AGM season in Australia generally showed a better skew to downgrades across the market. Positive contributors to performance over the month included GTN, Aurizon, NAB, Rio Tinto and BHP Billiton while Healthscope, Crown, Resmed and AMP detracted. During the month Radiate, a company which Fund holding GTN has an option to acquire, announced a 10-year deal with CBS Radio to supply it customised traffic data for its stations and websites. CBS Radio is the second largest owner and operator of radio stations in the US and should the GTN acquisition of Radiate proceed it will add a US arm to existing businesses in Australia, Canada, Brazil and the UK.

In terms of portfolio changes, the Fund removed AMP from the portfolio over the month. The company announced another large downgrade to Life earnings and a reinsurance deal with Munich Re. Despite management trying to draw a line under this ongoing issue, it is very difficult to determine whether the worst is over for the business given the scale of the recent deterioration in the Life Book and the anaemic flows in the Wealth Management business.

### PORTFOLIO MANAGER

Tama Willis

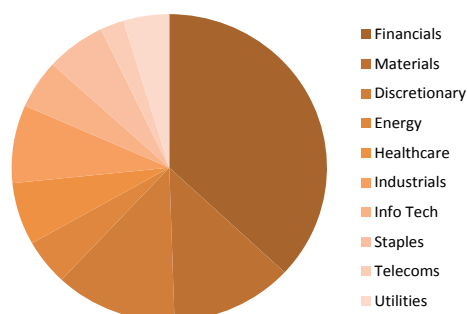


After a long period in international investment markets, Tama returned to NZ after a very successful career in London and Singapore to join Devon's investment team and holds responsibility for Devon's Australian and Trans Tasman Funds. Tama is widely regarded as a leading expert on resource and mining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

### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

|                     |        |
|---------------------|--------|
| Dual Listed         | 4.9%   |
| Australian Equities | 90.8%  |
| Cash                | 4.3%   |
|                     | 100.0% |
| Currency Hedge      | 0.0%   |

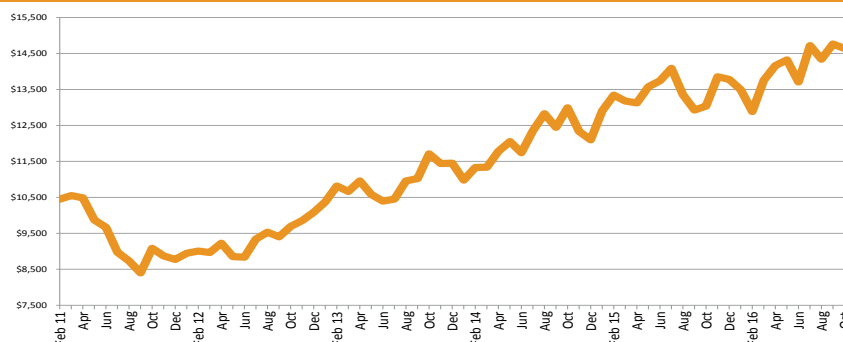
| PERFORMANCE                  | 1 Mth | 3 Mth | 1 Yr  | 3 Yr p.a | 5 Yr p.a |
|------------------------------|-------|-------|-------|----------|----------|
| As at 31/10/16               |       |       |       |          |          |
| Devon Australian Fund        | -0.9% | -0.6% | 12.3% | 7.7%     | 10.0%    |
| S&P/ASX200 Index Gross (NZD) | -1.1% | -2.3% | 7.0%  | 1.4%     | 4.8%     |

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

### Devon Australian Fund







### 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

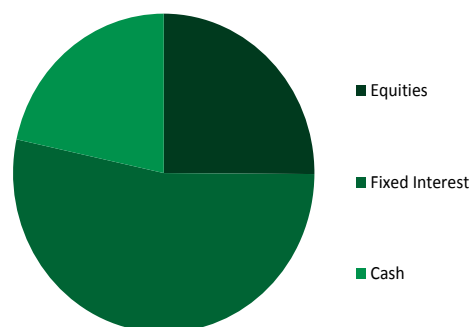
It was a challenging month for global bonds with yields rising steadily and the rate on US 10-year Treasuries trading up to their highest level since May 2016. The view globally is that a number of Central Banks, including the US Federal Reserve, have finished lowering their cash rates. In New Zealand though the situation is different with the short-end of our curve continuing to reflect a view that the RBNZ probably has one more cut left in this cycle.

The New Zealand corporate debt market continues to look reasonably healthy as evidenced by a number of issues occurring during the month and a number of others planned before year end. During October, Auckland International Airport raised NZ\$225m through an issue of 7-year unsecured unsubordinated bonds and ASB Bank launched a new offer of Tier two securities. Also over the course of the month the performance of the Diversified Income Portfolio was negatively affected by the sell-off in high yielding Australasian equities.

### KEY HOLDINGS



### ASSET ALLOCATION



### GROWTH

|             |       |
|-------------|-------|
| NZ Equities | 13.0% |
| AU Equities | 11.1% |

### DEFENSIVE

|                     |       |
|---------------------|-------|
| Cash                | 22.6% |
| NZ Corporate Bonds  | 53.3% |
| NZ Government Bonds | 0.0%  |

### PERFORMANCE

As at 31/10/16

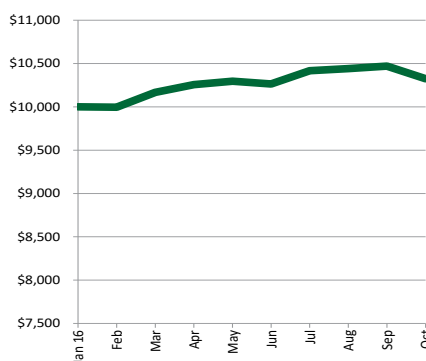
|                         | 1 Mth | 3 Mth | Inception |
|-------------------------|-------|-------|-----------|
| Diversified Income Fund | -1.4% | -0.9% | 4.4%      |
| OCR +1.5%               | 0.3%  | 0.9%  | 3.1%      |

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.

### NET PERFORMANCE

Based on \$10,000 invested at 1 January 2016

#### Devon Diversified Income Fund\*



\*Fund commenced on 1 January 2016

### AT A GLANCE

|                          |   |
|--------------------------|---|
| Targeted Portfolio Yield | 5.5%  |
| Commenced                | January 2016  |
| Total strategy           | \$5.6m  |
| Distributions            | Target distributions of 1.5 cents per unit after tax paid quarterly |

### 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 opportunities for his clients.



### 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.

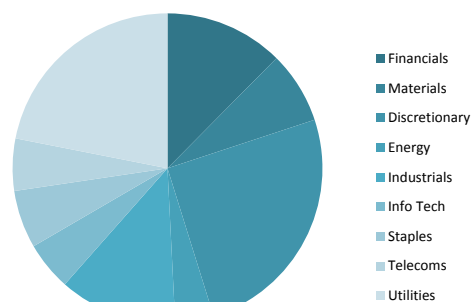
### DEVON DIVIDEND YIELD FUND

The Dividend Yield Fund's substantial allocation to the Australian market (43% at the beginning of the month) helped to mitigate the impact of the sell off in New Zealand. Within the New Zealand allocation it was difficult to escape what became a very broad based sell off. Interestingly Spark (formerly Telecom New Zealand), which pays one of the highest dividend yields in the New Zealand market and a substantial Fund holding, rose 1.4% over the month – an outcome that is to say the least inconsistent with the view that the selling was driven by the reversal of the "yield trade". The Fund's avoidance of some of the market's most expensive names (particularly Auckland Airport and Fisher and Paykel Healthcare) helped relative performance, but a very confusing trading update from Sky City saw that stock make the largest negative contribution for the month. In Australia the rail network and operations business Aurizon, which was added to the Fund in September, was a strong contributor.

### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

|                      |        |
|----------------------|--------|
| New Zealand Equities | 51.9%  |
| Australian Equities  | 44.2%  |
| Cash                 | 4.0%   |
|                      | 100.0% |
| Currency Hedge       | 99.9%  |
| Yield                | 6.0%   |

### PERFORMANCE

As at 31/10/16

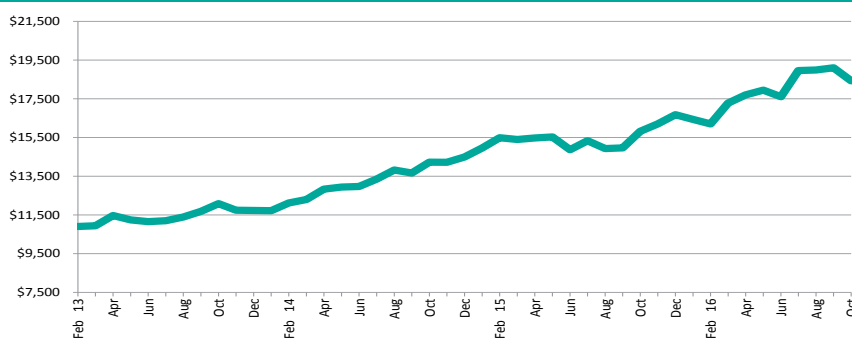
|                           | 1 Mth | 3 Mth | 1 Yr  | 3 Yr p.a | 5 Yr p.a |
|---------------------------|-------|-------|-------|----------|----------|
| Devon Dividend Yield Fund | -3.5% | -2.8% | 16.5% | 15.6%    | -        |
| TT Index (Hedged)         | -3.8% | -4.2% | 11.2% | 8.1%     | -        |

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

### Devon Dividend Yield Fund\*



\*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 Dividend Yield 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.



### 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

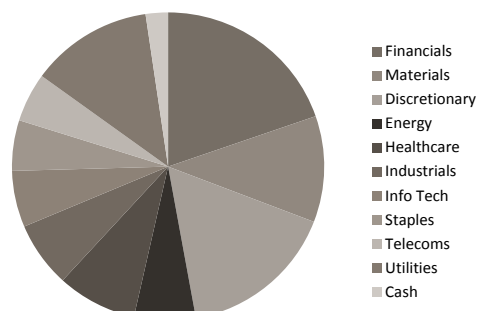
The Trans-Tasman Fund declined 3.1% over the month, outperforming the Trans-Tasman Index. The S&P/NZX50G index continued its second month of underperformance compared to the S&P/ASX200G with a number of the highly valued NZ companies like Auckland Airport and Fisher and Paykel being de-rated (the Fund is underweight both). In Australia, a strong performance from Fund holdings GTN, Aurizon and Rio Tinto was largely offset by a difficult month for Healthscope, Crown and Westfield Group.

The Fund reduced its position in Healthscope (HSO) following a disappointing AGM update. HSO is a leading private healthcare provider in Australia with 45 hospitals and 48 medical centres. At its AGM HSO reported a general slowdown in demand for its services in Q1 FY17 which put at risk EBITDA growth for the full year. An industry slowdown has also resulted in public hospitals chasing higher volumes from private patients. The Fund reduced the position given the risks to the medium term earnings profile and a rising net debt to EBITDA profile.

### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

|                      |        |
|----------------------|--------|
| New Zealand Equities | 46.9%  |
| Australian Equities  | 50.7%  |
| Cash                 | 2.3%   |
| Currency Hedge       | 0.0%   |
|                      | 100.0% |

| PERFORMANCE              | 1 Mth | 3 Mth | 1 Yr  | 3 Yr p.a | 5 Yr p.a |
|--------------------------|-------|-------|-------|----------|----------|
| As at 31/10/16           |       |       |       |          |          |
| Devon Trans-Tasman Fund  | -3.1% | -2.7% | 12.4% | 10.8%    | 13.6%    |
| Trans-Tasman Index Gross | -3.3% | -3.8% | 11.7% | 6.9%     | 10.3%    |

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

### PORTFOLIO MANAGER

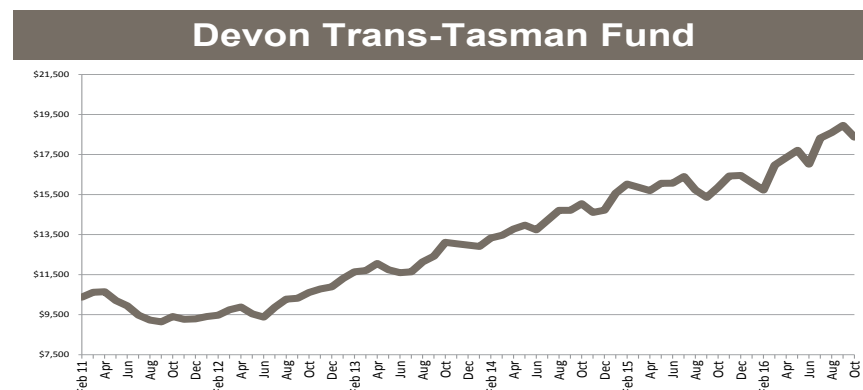
Tama Willis



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### NET PERFORMANCE

Based on \$10,000 invested at 1 January 2011







### GLOBAL THEMES FUND

### FUND OUTLINE

The Global Themes Fund invests in Global Financial Assets predominantly 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 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

October saw a fresh wave of nervousness and volatility enter global equity markets as we continued to edge closer to the US election on 8 November. This was particularly prevalent in sectors likely to be targeted by a Clinton-led government – like healthcare. As a result, exposure to European Pharmaceuticals and US Medical Devices detracted from our monthly performance. On the other hand, some of the dynamics we have been waiting for have started to show renewed signs of life – namely higher bond yields, and a weaker Japanese Yen. We are positioned for both of these themes, and this drove our strong performance this month. Given this, we remain comfortable with holding an elevated level of cash in the Fund.

Our highest conviction themes remain US Banks and Japan, which should perform well in an environment of continued rising US bond yields and a weakening Yen, respectively. A solid earnings season from the US banks has reiterated our conviction here. We also have significant exposure to the Technology sector, in which we see some exciting growth prospects.

We continue to believe that markets are under-pricing the risk of either a Trump upset, or a contested election, should Hillary Clinton win by a narrow margin. This, combined with

the elevated multiples many markets are trading on and a likely December interest rate hike in the US, leaves us seeing a greater risk of downside than upside in equities into the end of the year. In light of this, we plan to increase our cash holding in the fund prior to the election, funded by a temporary reduction in our US Banks exposure. This should help to insulate the fund in the event of any flight to safety (rally in bonds) on the back of a surprise election outcome.

### Returns

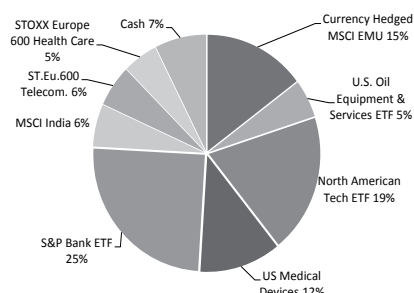
The Fund rose 0.9% in October to a unit price of \$2.2036. This compares with a

0.9% fall in our global equity benchmark. The Fund has risen 10.6% since inception in October 2014, versus a 12.9% increase in the iShares MSCI All Country World Index Exchange Traded Fund 50% hedged to NZD.

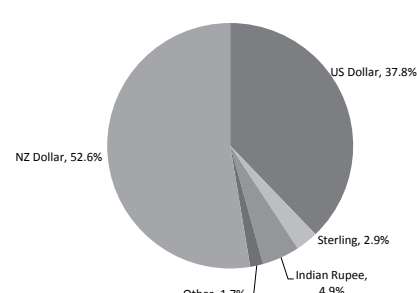
### Currency exposures

We maintained the currency hedge level in the fund at its benchmark weight of 50% throughout the month. We are comfortable with this position at present, however we are watching for opportunities to increase the hedge level given that we believe that the market is still overpricing the risk of further interest rate cuts from the RBNZ.

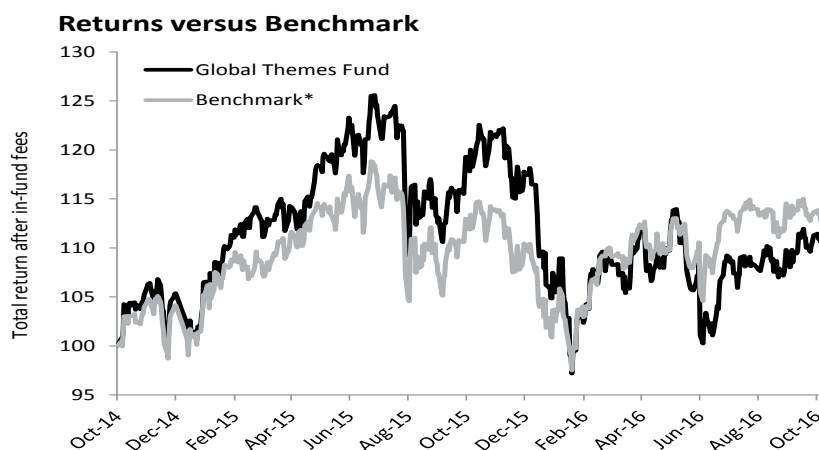
### SECTOR ALLOCATION



### 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

### 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 INFNZ 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.