

## MONTHLY REPORT

Keeping you up to date with Devon Funds and the markets

February 2018

### MARKET COMMENTARY

## It's All About the Milk

Last month the New Zealand share market witnessed an extraordinary event. The a2Milk Company (whose NZX code is ATM) announced their first-half result which, alongside a deal with Fonterra, resulted in their share price rallying almost 44%. Across financial markets this type of price performance in itself is not unprecedented, but what is almost unique with this situation is that this jump in price occurred, outside a takeover event, to our largest listed company. From its humble beginnings where, for example, ATM could be purchased for only 10 cents-per-share in early 2011 to today where it now trades at close to \$13 per share, this is a story that at the very least, captures the imagination. It now has a market capitalisation of \$9.4bn and is much larger than all our traditional listed businesses such as Auckland International Airport, Fletcher Building and Contact Energy.

The impact that ATM has had on the performance of the S&P/NZX50 Index (NZX50) and the outcomes for those responsible for investing money in this part of the world has been considerable. If we look back to February, the NZX50 finished the month down 0.81% but within this negative return was a positive contribution of 3.4% from ATM ... [Read More](#)



Devon is delighted to have won the Fund Manager of the Year: Domestic Equities Category, New Zealand 2017.

Thanks to all our clients for your on-going support.

Morningstar Awards 2017©. Morningstar, Inc. All Rights Reserved. Awarded to Devon Funds Management for Morningstar Fund Manager of the Year 2017, Domestic Equities Category, New Zealand. Further details on the Devon Investment Funds can be found in the Devon Product Disclosure Statement available at [www.devonfunds.co.nz](http://www.devonfunds.co.nz)

### MARKET INDICES

Index	Region	Monthly Return	1 Yr. Return
S&P/NZX50G	NZ	-0.8%	16.8%
S&P/ASX200G	AUSTRALIA	0.4%	10.1%
MSCI World Index	GLOBAL	-3.1%	19.2%
S&P500	USA	-2.6%	18.4%
FTSE100	UK	-3.4%	3.4%
NIKKEI 225	JP	-4.4%	17.6%
NZ 90 Day Bank Bill	NZ	0.2%	1.9%



AT A  
GLANCE

### UNIT PRICES

DEVON ALPHA FUND

**\$1.6428**

DEVON AUSTRALIAN FUND

**\$1.4113**

DEVON DIVIDEND YIELD FUND

**\$1.7470**

DEVON DIVERSIFIED INCOME FUND

**\$1.5375**

DEVON TRANS-TASMAN FUND

**\$3.6742**

GLOBAL THEMES FUND

**\$2.8063**

Prices as at 28 February 2018

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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](mailto:admin@devonfunds.co.nz) Website: [DevonFunds.co.nz](http://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.

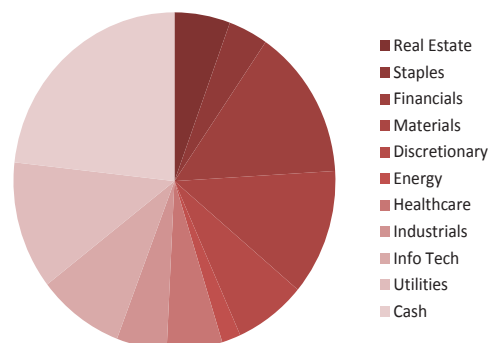
### DEVON ALPHA FUND

We were disappointed with the performance of the Alpha strategy during the month. Although we were holding a reasonably high level of cash, the portfolio generated a negative absolute return. Amongst the detractors were GTN, Fletcher Building and Contact Energy. Disappointingly, the share price of Vista Group also fell over the month despite reporting what we considered to be an excellent financial result (the stock did rise 8% on the day of the result). With Operating Profit for FY17 of \$20.4m and exciting growth prospects existing across Cinemas, data (Movio), and through the development of their Chinese business we believe that this investment will generate good returns for us over the next few years. A number of our companies did perform well over the month including Serko which rallied almost 12% and Spark Infrastructure which finished up 4%.

### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

New Zealand Equities	28.3%
Australian Equities	48.5%
Cash	23.2%
Total	100.0%
Currency Hedge	30.0%

### PERFORMANCE

As At 28/02/2018

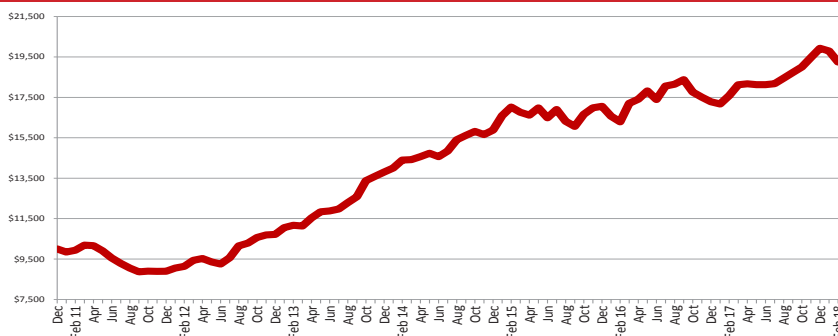
	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Alpha Fund	-2.8%	-1.1%	9.4%	3.9%	11.3%
OCR	0.2%	0.5%	2.0%	2.4%	2.6%

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



NOTE: Further information on the Devon Alpha Fund can be found in our Quarterly Fund Updates by visiting <https://devonfunds.co.nz/alpha-fund> or by clicking [HERE](#)

### PORTFOLIO MANAGER

Nick Dravitzki



Over the last decade Nick has specialised in investing in high yield equities and is Portfolio manager for the Devon Alpha, Diversified Income and Dividend Yield Funds. 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 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.

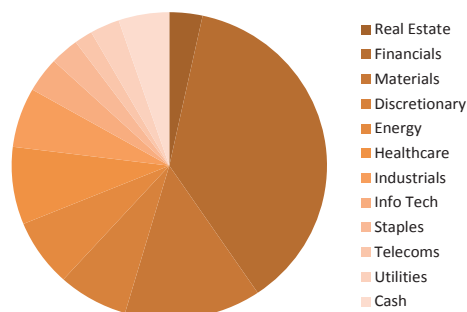
### DEVON AUSTRALIAN FUND

The Australian Fund underperformed over the month with its returns negatively impacted by our investments in GTN and the Super Retail Group. The GTN share price fell after the company announced their 1H18 results which saw revenue grow by 5.1% but reported profit fall after losses grew in their US division. Company management have acknowledged the challenges that exist in the US and have committed to either driving their operating costs down by renegotiating their current station contracts with CBS Radio or if this strategy is unsuccessful they will look to exit this business altogether. On a more positive note, this strategy enjoyed some strong returns from our investments in Rio Tinto and Spark Infrastructure. CSL Limited also performed well, finishing the month up over 11% after announcing a 1H18 result which saw company revenue grow by 11% and net profit lift by 31%.

### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

Dual Listed	3.7%
Australian Equities	91.1%
Cash	5.2%
Total	100.0%
Currency Hedge	0.0%

### PERFORMANCE As At 28/02/2018

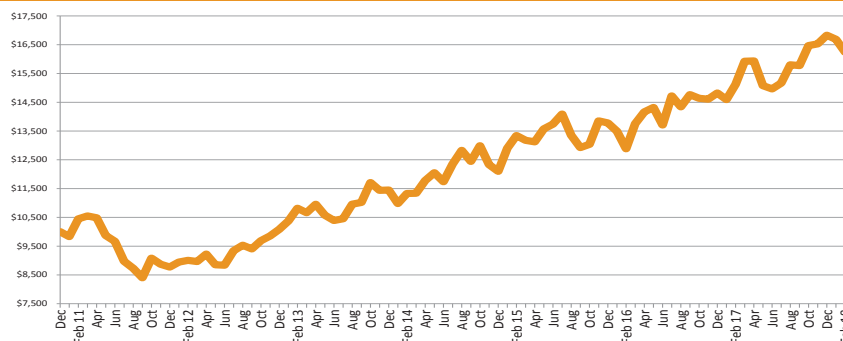
	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Australian Fund	-2.7%	-1.8%	7.4%	6.8%	8.5%
ASX200 Index Gross (NZD)	-1.0%	-0.8%	11.7%	6.6%	5.1%

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



NOTE: Further information on the Devon Australian Fund can be found in our Quarterly Fund Updates by visiting <https://devonfunds.co.nz/australian-fund> or by clicking [HERE](#)

### 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.





### 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

Global interest rates continued to rally in February with the US 10-year Treasury yield finishing the month at 2.86%. This did not flow through to any significant repricing of local interest rates though and the spread between the New Zealand Government 10-year bond and its US equivalent closed to its smallest spread ever, of 0.05%. On average over the past decade the average spread between these two interest rates has been 1.76%. Both the RBNZ and Reserve Bank of Australia met during February to discuss monetary policy and in both cases rates were left unchanged and there was no sense of policy tightening from either camp in the near term. In the US, the new Fed Chairman, Jerome Powell, made a number of optimistic comments on the US economy although he did retain his view that any future rate increases will be implemented gradually.

### PORTFOLIO MANAGER

Nick Dravitzki



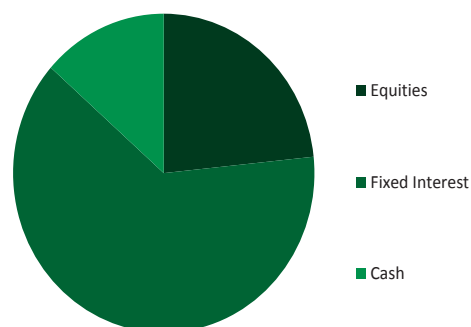
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### KEY HOLDINGS



### ASSET ALLOCATION



### GROWTH

NZ Equities	8.4%
AU Equities	14.6%

### DEFENSIVE

Cash	13.8%
NZ Corporate Bonds	63.2%
NZ Government Bonds	0.0%

### PERFORMANCE

As At 28/02/2018

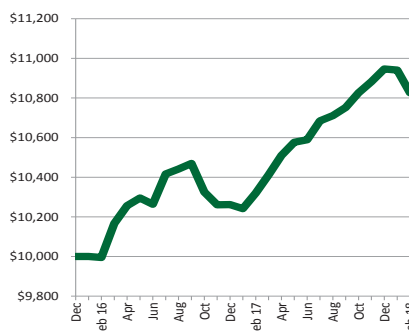
	1 Mth	3 Mth	1 Yr	2 Yr
Devon Diversified Income Fund	-1.0%	-0.5%	4.8%	4.5%
OCR + 1.5%	0.3%	0.9%	3.5%	3.6%

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

NOTE: Further information on the Devon Diversified Income Fund can be found in our Quarterly Fund Updates by visiting <https://devonfunds.co.nz/diversified-income-fund> or by clicking [HERE](#)

### AT A GLANCE

Targeted Portfolio Yield	5.0%
Commenced	January 2016
Total strategy	\$5.04m
Distributions	Target distributions of 1.5 cents per unit after tax paid quarterly



### 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.

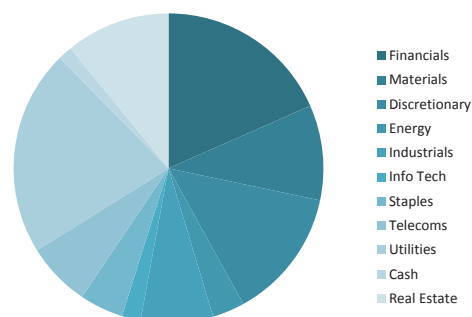
### DEVON DIVIDEND YIELD FUND

In February members of our investment team travelled to Australia to meet with a number of the companies in the Dividend Yield strategy. These included Spark Infrastructure Group and Suncorp whose share prices rallied 4.3% and 1.7% respectively after announcing their financial results. Spark is a major infrastructure company that primarily invests in regulated electricity businesses in Victoria and South Australia and during FY17 this company produced operating cash flow of \$645m and achieved strong working capital performance. During our meeting with management we spoke at length about the high quality asset base that Spark has developed, their successful cost management program and the opportunity for dividend growth looking forward. Detractors from the portfolio's returns included our investments in Metro Performance Glass, Z Energy and Mercury New Zealand whose share prices all fell during the month.

### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

New Zealand Equities	36.0%
Australian Equities	62.6%
Cash	1.5%
Total	100.0%
Currency Hedge	96.0%
Yield	6.40%

### PERFORMANCE

As At 28/02/2018

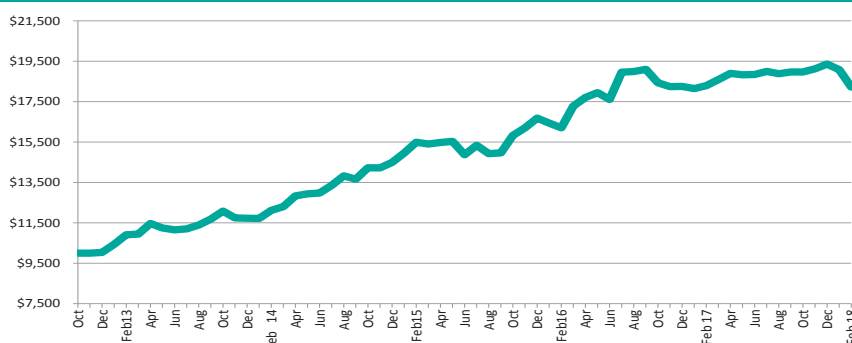
	1 Mth	3 Mth	1 Yr	3 Yr p.a
Devon Dividend Yield Fund	-4.5%	-4.7%	-0.6%	5.5%
TT Index (Hedged)	-0.2%	2.0%	13.5%	8.8%

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\*



NOTE: Further information on the Devon Dividend Yield Fund can be found in our Quarterly Fund Updates by visiting <https://devonfunds.co.nz/dividend-yield-fund> or by clicking [HERE](#)

### PORTFOLIO MANAGER

Nick Dravitzki



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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 most significant contributor to the underperformance of the Trans-Tasman strategy during the month was the extraordinary returns generated by a2Milk. This company rallied almost 44% in February and is up 460% over the past 12-months. Although we commend company management for their success, at Devon we have maintained an underweight position in this stock due to concerns over the sustainability of a2Milk's sales channel into China. We will continue to monitor this business closely and have two of our analysts in China during March reviewing the situation. Fletcher Building also weighed on performance after the company announced further provisioning in their Construction division. Offsetting these investments were our holdings in CSL, Spark Infrastructure and Woolworths that all rallied after reporting strong financial results. Another of our largest investments, Vista Group, also delivered encouraging FY17 numbers that saw their revenue and operating profit grow by 20% and 57% respectively.

### PORTFOLIO MANAGER

Tama Willis



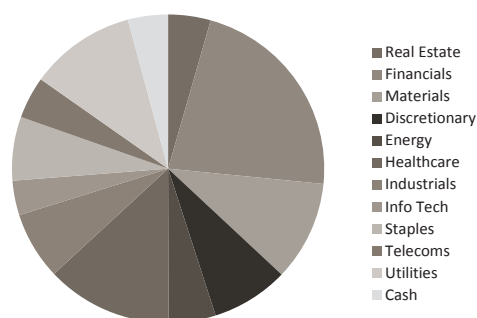
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### KEY HOLDINGS



### ASSET ALLOCATION



### GEOGRAPHIC ALLOCATION

New Zealand Equities	47.9%
Australian Equities	47.9%
Cash	4.2%
Total	100.0%

### PERFORMANCE

As At 28/02/2018

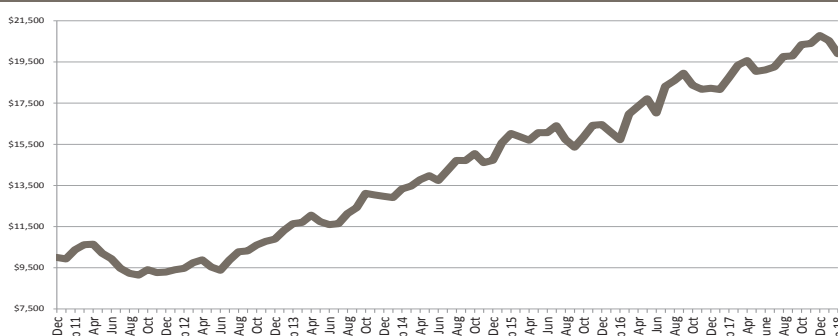
	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Trans-Tasman Fund	-3.1%	-2.4%	6.2%	6.4%	10.7%
Trans-Tasman Index Gross	-0.9%	0.7%	14.3%	9.5%	9.6%

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

### Devon Trans-Tasman Fund



NOTE: Further information on the Devon Trans-Tasman Fund can be found in our Quarterly Fund Updates by visiting <https://devonfunds.co.nz/trans-tasman-fund> or by clicking [HERE](#)





### 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

The sell-off in the bond market is finally beginning to rattle equity investors. The ~500 day streak without a 3% daily decline in the S&P 500 ended in February. Concerns that inflation will push the Federal Reserve into an aggressive tightening cycle were behind the weakness.

We believe the market is right to be wary of interest rates continuing to rise. The US economy is firing on all cylinders and the need for abnormally low interest rates has passed. That said, we don't think inflation is about to run amok. Accordingly 10 year Treasuries in the 3.00-3.50% range strike us as 1. perfectly reasonable given the state of the economy; and 2. unlikely to derail the bull market in equities.

Our US banks holding provides some insulation in a rising rate environment. Technology has been pleasingly resilient as well, and we remain happy holding a significant weight in this theme.

Our European Telecom theme is the most exposed to rising interest rates and was a drag on performance in February. However we continue to like this theme and saw good delivery of earnings from the major names in February. We are also seeing evidence of regulatory relief, for example Ofcom's determination on wholesale broadband pricing released last month was better than expected for BT Group's infrastructure division, Openreach.

This month I will be spending two weeks off

### 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 INFIZ 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.

shore talking to our research providers and fellow investors in Asia, Europe and the US. We are not anticipating dramatic changes to our portfolio, but this will be a welcome opportunity to test and refresh our conviction.

### Returns

The Global Themes Fund fell 2.6% in February, finishing the month at a unit price of \$2.8063. This compares with a 3.4% decline in our global equity benchmark.

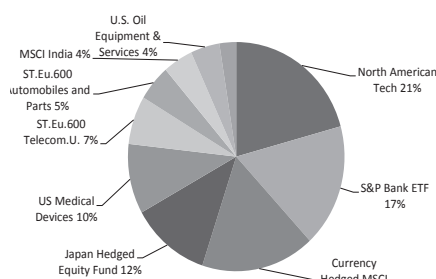
Our fund has risen 10.7% per annum since inception net of fees, versus 12.1% growth in the iShares MSCI All Country World Index

Exchange Traded Fund (50% hedged to NZD).

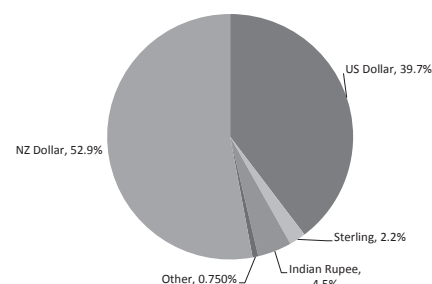
### Currency exposures

We continue to hold the currency hedge level in the fund at its benchmark weight of 50%. The Kiwi has been volatile but within a narrow range over recent months. We remain long US dollars in our themes, which was a drag over 2017. However we still see some defensive appeal from the greenback in a rising interest rate environment.

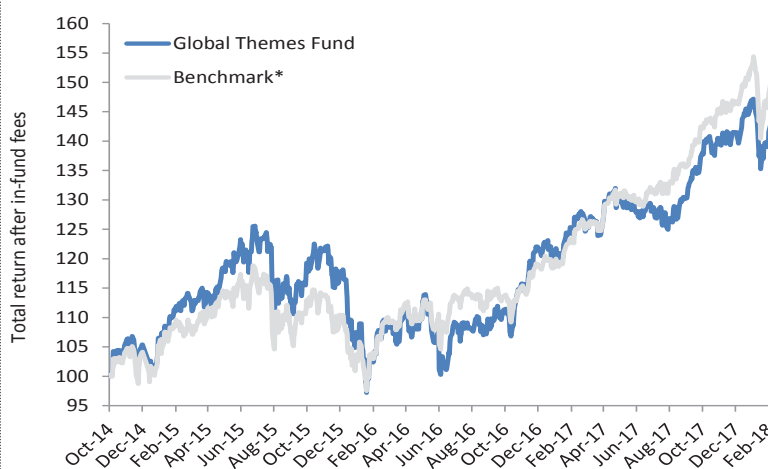
### SECTOR ALLOCATION



### CURRENCY EXPOSURE



### NET PERFORMANCE SINCE INCEPTION Returns versus Benchmark



\* iShares MSCI All Country World Index ETF. 50% hedged to NZD

NOTE: Further information on the Devon Global Themes can be found in our Quarterly Fund Updates by visiting <https://devonfunds.co.nz/global-themes-fund> or by clicking [HERE](#)