

MARKET COMMENTARY

NZ Housing Market – Correction or Crash

It appears very likely that the New Zealand housing market will turn down – the question now is whether it will be a correction or a crash?

In the decade since the GFC, most asset prices have risen strongly. The actions of global central banks in cutting interest rates to historical lows and printing vast amounts of money have resulted in solid global economic growth, but the availability of very cheap money has also driven the prices of shares, bonds and residential property to record levels.

In recent months though we have seen the return of volatility, and the confidence levels of investors, businesses and consumers are being tested. Notwithstanding the dramatic changes that we saw across equity markets during October, some of the more concerning data points that we have observed recently are in relation to residential property. Recent data shows that property prices are now falling sharply in many cities including in Sydney, Melbourne, London, New York and Vancouver... [Read More](#)

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MARKET INDICES

Index	Region	Monthly Return	1 Yr. Return
S&P/NZX50G	NZ	-6.4%	7.4%
S&P/ASX200G	AUSTRALIA	-6.6%	-0.1%
MSCI World Index	GLOBAL	-7.3%	1.7%
S&P500	USA	-6.8%	7.3%
FTSE100	UK	-4.9%	-0.9%
NIKKEI 225	JP	-9.0%	1.6%
NZ 90 Day Bank Bill	NZ	0.2%	1.9%



AT A
GLANCE

UNIT PRICES

DEVON ALPHA FUND

\$1.7019

DEVON AUSTRALIAN FUND

\$1.4114

DEVON DIVIDEND YIELD FUND

\$1.7884

DEVON DIVERSIFIED INCOME FUND

\$1.5398

DEVON TRANS-TASMAN FUND

\$3.7393

GLOBAL THEMES FUND

\$2.7677

Prices as at 31 October 2018

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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.

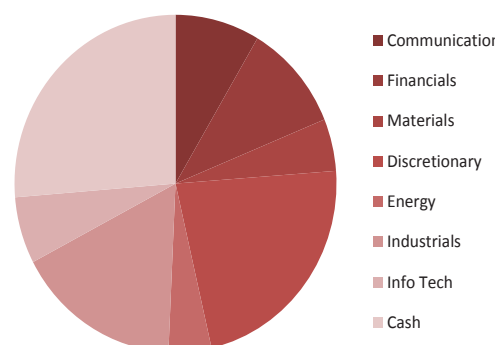
DEVON ALPHA FUND

The Alpha Fund's significant cash allocation (which sat at 42% at the end of September) helped the Fund perform materially better than underlying equity markets over October. Although the equity holdings in Alpha were unable to escape the negative effects of what was a sharp and very broad sell-off, we were nevertheless pleased to see that the defensive composition of the Fund helped protect investor capital. Several of the names in the portfolio proved very resilient over the month including Brambles and Atlas Arteria, but the standout was PWR Holdings which rose an astonishing 18%, helped by a positive trading update at the company's AGM. Super Retail was the most disappointing performer which suffered from a combination of a trading update which highlighted modestly slower sales growth and the resignation of its CEO. We have taken the opportunity afforded by lower prices during the month to invest some of the Fund's cash, adding BHP and Trade Me in recent days.

KEY HOLDINGS



ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

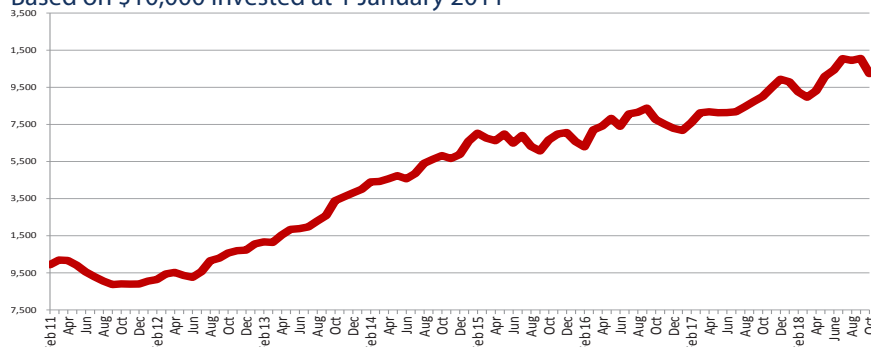
New Zealand Equities	15.4%
Australian Equities	58.3%
Cash	26.3%
Total	100.0%
Currency Hedge	27.00%

PERFORMANCE	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
As At 31/10/2018					
Devon Alpha Fund	-3.9%	-3.8%	8.2%	6.9%	8.8%
Official Cash Rate	0.2%	0.4%	1.8%	1.9%	2.4%

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

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.

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](#)



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 its benchmark during October. Our investment in PWR Holdings was a particular highlight for this strategy with shares in the company rallying 18%. PWR Holdings Limited (PWH) is an Australian-based company involved in the design and the production of customised cooling solutions for motorsports and the automotive industry. PWH has a greater than 50% market share in cooling systems for Formula 1 racing cars, an area where it continues to take market share. PWH also provided more detail on its long term strategy at a recent AGM including a focus on battery and electronics cooling for new customers across a diverse range of industries, aerospace and military among them. Other investments that also contributed positively to performance included Spark Infrastructure, QBE and Scentre Group. The volatility that we saw across the Australian market during the month has also provided some interesting new opportunities for us to further investigate.

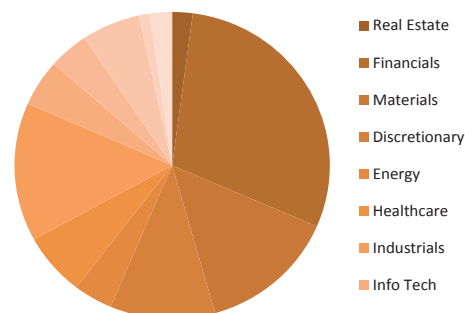
KEY HOLDINGS



GTN



ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

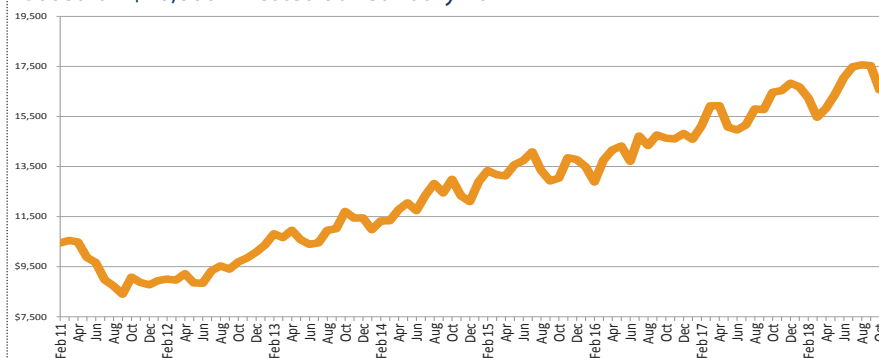
Australian	92.8%
New Zealand	4.9%
Cash	2.4%
Total	100.0%
Currency Hedge	0.0%

PERFORMANCE As At 31/10/2018	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Australian Fund	-5.5%	-5.3%	2.8%	9.1%	7.6%
ASX200 Index Gross (NZD)	-6.6%	-6.5%	-0.2%	9.3%	4.9%

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



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.

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](#)



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.

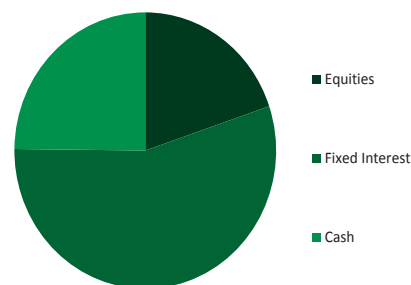
DEVON DIVERSIFIED IN- COME FUND

October proved to be a volatile month for the fixed interest markets, against a backdrop of equity markets weakness. In the US, the 10-year treasury yield finished the month at 3.13% although its intra-month rate reached a high of 3.24%. Against this backdrop junk bonds were particularly out of favour with yields rising significantly as investors looked to reduce their risk exposure. As expected the US Federal Reserve lifted the Federal Funds Rate by 0.25% and the market is pricing in a high probability of another hike before year-end. This action resulted in condemnation by Donald Trump of the Fed Chairman, Jerome Powell, and his monetary policy. New Zealand inflation data was stronger than expected with third-quarter CPI reported at 0.9%. A significant contribution to this came from Oil and Transport costs after the introduction of petrol taxes. The next RBNZ meeting is in early November, with expectations that rates will be left unchanged.

KEY HOLDINGS



ASSET ALLOCATION



GROWTH

NZ Equities	12.9%
AU Equities	6.9%

DEFENSIVE

Cash	24.8%
NZ Corporate Bonds	55.4%
NZ Government Bonds	0.0%

PERFORMANCE

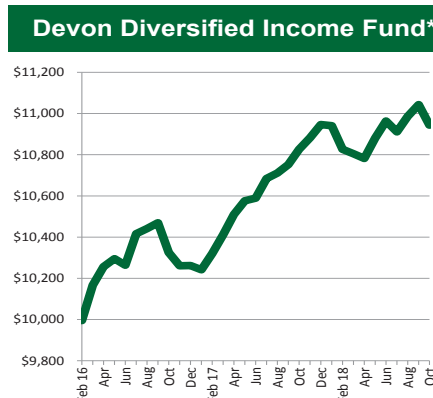
As At 31/10/ 2018

	1 Mth	3 Mth	1 Yr	2 Yr p.a
Devon Diversified Income Fund	-0.9%	0.3%	3.1%	3.9%
OCR + 1.5%	0.3%	0.8%	3.3%	3.3%

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



AT A GLANCE

Targeted Portfolio Yield	5.0%
Commenced	January 2016
Total strategy	\$6.45m
Distributions	Target distributions of 1.5 cents per unit after tax paid quarterly

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.

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](#)



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 focus on higher yielding equities generally skews its focus to the more traditionally defensive sectors like utilities and listed property, and this helped it to modestly outperform the market over October. In a month where any positive performance was a rarity, the solidity of many of these names (notably the Australian electricity distribution business Spark Infrastructure, the retail mall owner Scentre Group and electricity generator and retailer Mercury Energy) was very welcome. Most of the stock movements across the market were driven less by news flow than by broader (largely negative) sentiment, but in the case of Mercury its returns were helped by a positive operational update. This company's earnings have benefitted from relatively high generation volumes and, being slightly "long" generation (i.e. it generates more electricity than it provides in retail sales), it is able to benefit from currently elevated wholesale electricity prices.

KEY HOLDINGS

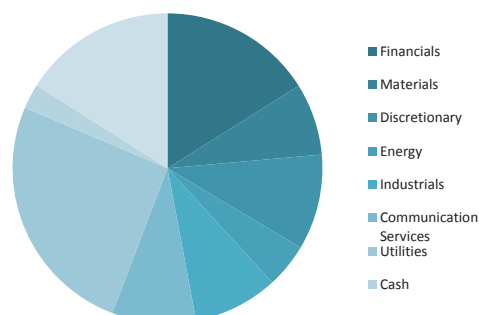
trademe



atlasArteria

SCENTRE GROUP

ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

New Zealand Equities	63.4%
Australian Equities	34.0%
Cash	2.6%
Total	100.0%
Currency Hedge	95.0%
Yield	7.34%

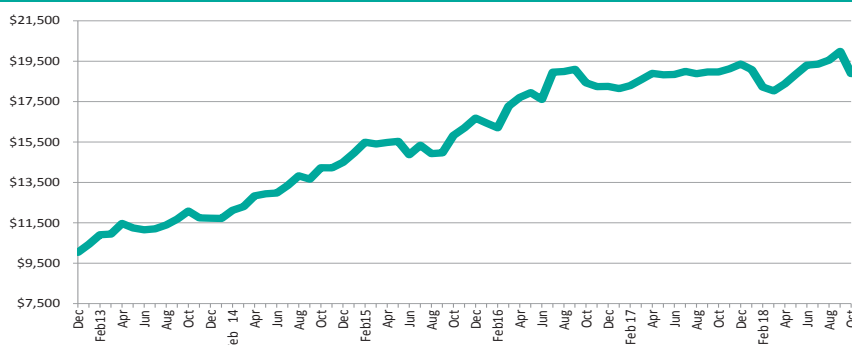
PERFORMANCE	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
As At 31/10/2018					
Devon Dividend Yield Fund	-5.5%	-2.4%	2.2%	6.9%	10.2%
TT Index (Hedged)	-6.2%	-4.0%	5.2%	10.9%	9.1%

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*



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

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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 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.

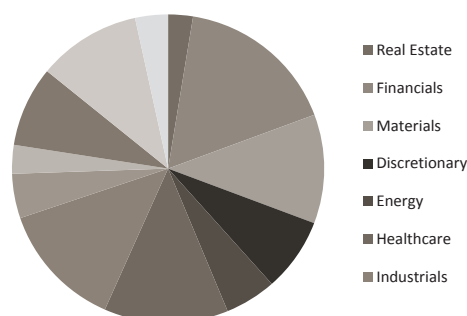
DEVON TRANS-TASMAN FUND

In a difficult market environment, we were pleased that this Fund performed ahead of its benchmark. The investments that made the most notable contributions to relative performance included Scentre Group, GTN, Atlas Arteria and Brambles. We were encouraged that key holding, Brambles, delivered solid first quarter constant currency revenue growth of 6%. Guidance from the company assumes a flat profit performance in the first half of 2019 before an acceleration in growth later that year. We see improving profitability beyond this period along with either a trade sale or demerger of their subsidiary, IFCO. The Fund also added to BHP over the month after its share price had recently fallen. We believe there are a number of positive catalysts ahead for this business. Firstly, the company is expected to announce a >US\$10bn capital return when the proceeds are received from the sale of the group's US on-shore oil and gas assets and secondly, the strength in iron ore and coking coal prices suggest upside to earnings.

KEY HOLDINGS



ASSET ALLOCATION



GEOGRAPHIC ALLOCATION

New Zealand Equities	46.4%
Australian Equities	50.2%
Cash	3.4%
Total	100.0%

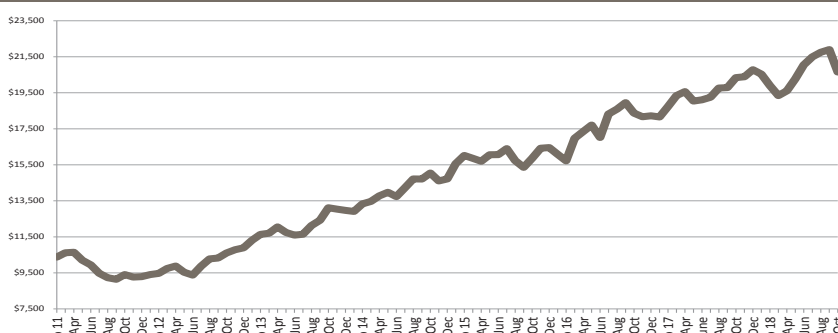
PERFORMANCE As At 31/10/2018	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a
Devon Trans-Tasman Fund	-5.7%	-3.9%	3.7%	8.9%	9.3%
Trans-Tasman Index Gross	-6.5%	-4.2%	3.6%	11.4%	8.6%

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](#)

PORTFOLIO MANAGER

Tama Willis



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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

What began as equity markets pricing in a rapid 40bp move higher in bond yields at the beginning of the month, morphed into a ~10% sell-off (at its worst point) as the month progressed, on the back of fears of a slowdown in growth against a hiking Fed. October has been our third >5% sell-off this year. While this may sound frightening at first blush, since the GFC market trough the S&P 500 has had 18 of them, ~2 per year on average. At the same time, equities have risen more than 15%p.a. So semi-annual pull backs are the norm. Rather, it was 2017, with no major sell-offs and historically low volatility, that should be viewed as unusual. So how has our outlook changed? In short, it hasn't. Economic and corporate fundamentals remain sound, and recession risk over the next 12 months remains low in our view. Courtesy of poor returns and positive earnings growth, equities have become more attractively priced. Accordingly, we are hunting for opportunities rather than running for the hills.

Earnings season is well underway, with more than 50% of US companies having now reported. Earnings growth is running at around 24% yoy currently, ahead of our expectations. Revenue growth is tracking at just below around 10% yoy. We're happy with this. At this stage in the cycle, however, investors are less interested in whether or not the last quarter has been good (it's more or less taken for granted that it will be), and more emphasis is put on revenue outlook (i.e. how long will the good times last?) – hence the post-earnings release moves in some stocks (e.g. Amazon). However, while some company guidance has missed

consensus expectations, absolute growth is still forecast to be reasonably strong.

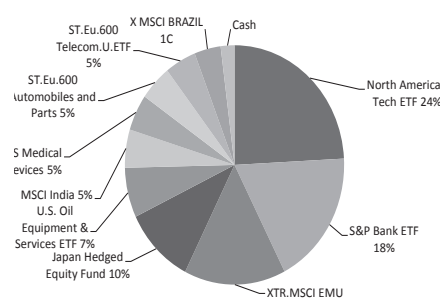
RETURNS

The Global Themes Fund fell 7.9% in October, finishing the month at a unit price of \$2.7677. This compares with a 6.7% fall in our global equity benchmark, in what was the worst month for equity markets in around six years. Our fund has risen 8.5% per annum since inception net of fees, versus 10.1% per annum growth in the iShares MSCI All Country World Index Exchange Traded Fund (50% hedged to NZD).

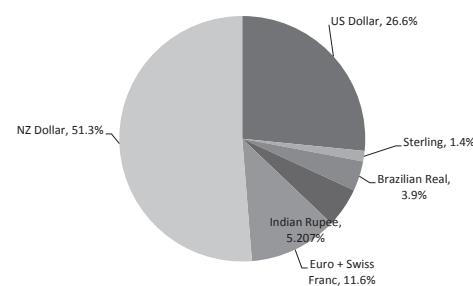
CURRENCY EXPOSURES

The currency hedge level in the fund remains at its benchmark weight of 50%, which we are comfortable with for now. However, we continue to keep a close eye on local economic data and movements in the currencies of our key trading partners. NZD/USD below 0.64 would likely see us closer to increasing our hedging ratio benchmark weight of 50%, which we are comfortable with for now. However, we continue to keep a close eye on local economic data and movements in the currencies of our key trading partners.

SECTOR ALLOCATION

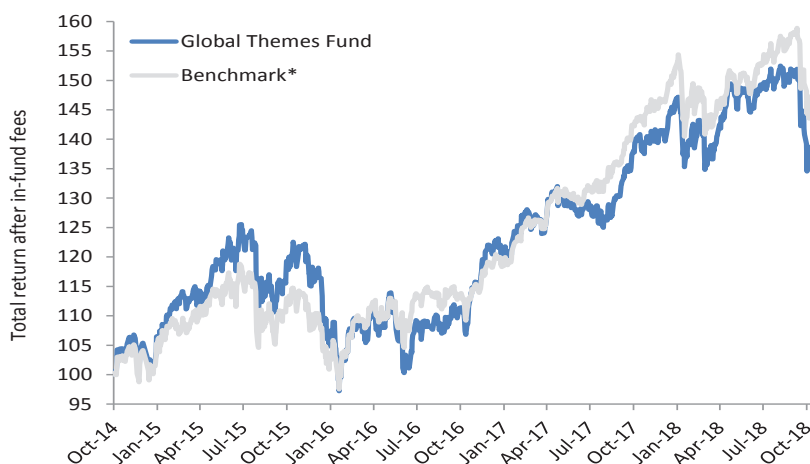


CURRENCY EXPOSURE



NET PERFORMANCE SINCE INCEPTION

Returns versus Benchmark



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](#)

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.