



# Qualitative Fund Research

Devon Global Themes Fund

October 2018

## About the Manager

Devon Funds Management Limited (Devon, the Manager) has provided a comprehensive profile which is available [here](#). Devon was established in 2010, and has proven to be successful in growing its business in institutional and retail funds management. Devon has partnered with JBWere (NZ) Pty Ltd (JBWere or the Investment Adviser), who provide a profile of JBWere [here](#).

Devon takes its fiduciary duty to clients very seriously. The Manager believes it has an obligation to ensure that the businesses it invest into conduct themselves in accordance with the highest governance standards.

Devon outlines its values and views on the expectations of businesses it invests in, viewing good corporate citizenship, stakeholder interest and sustainability as being the foundation of good business sense, available [here](#). FundSource views corporate citizenship and governance frameworks as extremely important foundations from which a manager starts to engage with the client experiences.

Understanding clients is at the heart of any business and is critical to the longevity of an investment manager. Devon has a clearly articulated statement on Client Care [here](#).

## Using this Fund

**This is General Advice only and should be read in conjunction with the Disclaimers, Disclosures and Warnings at the end of this document.**

The Global Themes Fund (“the Fund”) provides investors with exposure to global equities, predominantly via a portfolio of ETF’s and index funds that look to replicate a theme. The Fund is expected to be fully invested, with cash being held to manage daily cashflows and covering any derivative positions.

The Fund is predominantly exposed to global companies and themes, as determined by the Investment Adviser, and approved by the Manager. Investors should be aware that the Fund may experience periods of negative returns and that

Devon manages a range of funds including:

- Devon Alpha Fund
- Devon Australian Fund
- Devon Dividend Yield Fund
- Devon Diversified Income Fund
- Devon Trans-Tasman Fund
- [Global Themes Fund](#); and
- Wholesale Funds

The funds above are managed by four Portfolio Managers who, together with an additional investment analyst are also responsible for sector research. In the case of the Global Themes Fund (the Fund), Devon is the Manager, managing the Fund via its Investment Committee, and is ultimately responsible for the Fund. Devon employs the services of JBWere, who act in the capacity of Investment Adviser. Biographies for key JBWere personnel can be found [here](#). Devon’s operations team consists of six people plus the Managing Director. For the number of funds being managed this is a small team of well tenured and experienced personnel. Individual bios on the team at Devon can be found [here](#).

there is a risk of potential capital loss being incurred on their investment. The Fund is suitable for investors with an investment horizon of more than five years.

The Fund intends to be fully invested, however cash can range from 0%-20%. Currency hedging can range from 0-100%, is typically 50% hedged, and may enter into forward currency and other derivative contracts to manage foreign currency risk.

The Fund is a Portfolio Investment Entity (PIE) and the Manager does not intend to pay distributions. Any income received is reflected in the Funds unit price. The Fund, can however, pay a distribution at the Manager's discretion, semi-annually.

Question	What the Manager says	What FundSource thinks																
<p>What are the Manager's assets under management - in total and in this Fund?</p>	<p>As at June 2018 Devon Funds Management (the Manager) had about \$2.3 billion under management on behalf of a diverse range of New Zealand clients, including; the New Zealand Superannuation Fund, Community Trusts, charities, KiwiSaver schemes, corporates pension schemes and individual investors.</p> <p>As at 30 June 2018:</p> <table border="0"> <tr> <td>Alpha Fund:</td> <td>\$ 136.01M</td> </tr> <tr> <td>Australian Fund:</td> <td>\$ 16.3M</td> </tr> <tr> <td>Diversified Income Fund:</td> <td>\$ 5.7M</td> </tr> <tr> <td>Dividend Yield Fund:</td> <td>\$ 185.06M</td> </tr> <tr> <td>Trans-Tasman Fund:</td> <td>\$ 279.40M</td> </tr> <tr> <td>Global Themes Fund:</td> <td>\$ 68.2M</td> </tr> <tr> <td>Mandates</td> <td>\$1,501.65M</td> </tr> <tr> <td><b>Manager Total FUM:</b></td> <td><b>\$2,290.22M</b></td> </tr> </table>	Alpha Fund:	\$ 136.01M	Australian Fund:	\$ 16.3M	Diversified Income Fund:	\$ 5.7M	Dividend Yield Fund:	\$ 185.06M	Trans-Tasman Fund:	\$ 279.40M	Global Themes Fund:	\$ 68.2M	Mandates	\$1,501.65M	<b>Manager Total FUM:</b>	<b>\$2,290.22M</b>	<p>The business as a whole has significant funds under management across its six strategies.</p> <p>Global equities form a core component of a diversified portfolio. There are advantages to New Zealand investors accessing the global equities via PIE structure. Devon via its Global Themes Fund offers investors with exposure a range of macro, sector, country and regional themes.</p> <p>The Global Themes Fund commenced on 17 October 2014, and has attracted reasonable support, raising over \$68 million in less than three years.</p>
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<p>Who is accountable for managing the Fund, and how long has the investment team worked together?</p>	<p>JBWere is the Investment Adviser for this strategy. JBWere, comprises two key team members, Bernard Doyle, JBWere Executive Director Investment Strategy Group, and Andrew Thompson, Investment Analyst. JBWere is responsible for making the investment recommendations for this Fund with Devon overseeing all decisions.</p> <p>Doyle oversees New Zealand equity strategy and global tactical asset allocation for JBWere's private and institutional clients. He also co-leads the JBWere Investment Strategy Group. Before joining JBWere, Bernard was the New Zealand equity strategist for Goldman Sachs &amp; Partners.</p> <p>Thompson joined JBWere's Investment Strategy Group at the start of 2016, with a focus on global equity strategy. Before joining JBWere, Andrew was an Investment Analyst at BNZ Private Bank, and prior to that a Supervisor in the audit division at KPMG.</p>	<p>FundSource holds a strong positive view on the senior investment and executive management team at Devon. Devon have been expanding the analyst and operations teams. Devon appointed Mark Brown in the role of Chief Investment Officer (CIO), commencing in January 2018. Brown has also assumed responsibility of Investment Committee Chair, succeeding current Managing Director, Robertson. FundSource views the upcoming appointment of Brown positively. FundSource notes that Portfolio Managers (PM) Willis and Dravitzki have increased the number of funds they are responsible for over the course of 2016 ad 2017.</p> <p>The Investment Adviser has a team of two people who directly engage with Devon, for this Fund. The New Zealand team is led by Investment Strategist Doyle, who is supported by an investment analyst, Thompson. Doyle places a strong emphasis on macroeconomic and thematic investing. FundSource is aware that Doyle and Thompson are able to leverage the broader JBWere strategy team, which consists of ~15 staff across Australia and New Zealand.</p> <p>The Investment Adviser's primary role is to develop themes, and determine the appropriate way to gain access to each investment thematic. JBWere utilises a range of international research partners to ensure access to global investment intelligence. The Manager's appointment of an Investment Adviser is viewed positively by FundSource.</p>																
<p>What objective is the Manager trying to achieve?</p>	<p>The investment objective of the allocation to global financial assets is to outperform the Benchmark (the MSCI All Country World Index exchange traded fund 50% hedged to New Zealand dollars) after management fees.</p>	<p>The Fund aims to generate greater returns than its benchmark, via a portfolio of global equities, based around a series of themes. The Investment Adviser also looks to keep themes relatively simple, to ensure investments are readily available, via ETF's and indices. As the Fund is thematic in nature investors should be aware that the Fund's asset allocation may not reflect</p>																

		<p>the sector allocation or weights in the reference benchmark, the MSCI All Country World Index.</p> <p>FundSource notes that the reference index is hedged at 50%, which is aligned to the Managers expected 50% portfolio hedging. The Fund's hedging can range between 0-100%, which can positively or negatively contribute to the Funds overall performance.</p> <p>With an inception date of September 2014, the current performance history is short, preventing FundSource from forming a strong objective view on the Manager's ability to consistently produce a solid investment return for investors. FundSource notes the Investment Adviser's history for the strategy pre-dates this Fund, with an inception date of March 2005. The strategy has performed in line with its benchmark since inception. Importantly FundSource highlights historic performance is no guarantee of future performance. However, does provide some indication as to how successfully the manager has implemented its ideas, and the results of those decisions. Investors should expect the Fund to be generally fully invested, and this will be heavily dominated by ETFs and index funds, rather than direct securities.</p> <p>The Manager reports performance on a net of fees basis, as detailed in the Fund's <a href="#">monthly reports</a>. FundSource notes that reference benchmarks do not typically consider fees or taxes. Additional performance information can be found on <a href="#">Disclose website</a>.</p>
<p>What does the Manager invest your money into?</p>	<p>The Fund invests in a carefully selected portfolio of global financial assets and cash. These assets may include Exchange Traded Funds, listed equity securities, index funds, futures contracts, currency positions and derivative securities.</p>	<p>The Fund invests in a portfolio of global financial assets and cash. The Fund will mostly invest via ETFs, and index funds. However, FundSource notes that the Fund can also invest in listed equity securities, futures contracts, currency positions and derivative securities. FundSource highlights that while passive investment structures are predominantly used to gain exposure to a theme, the Fund is actively managed. The Fund does not look to replicate the composition of its performance reference benchmark, at either the security or sector level. Therefore, portfolio holdings and investment returns may differ considerably from the Fund's benchmark.</p> <p>The Fund is suitable for investors who want an actively managed global equity portfolio, that looks to employ both macro and fundamentally driven themes. The themes can be quite narrow or broad, and reflect the Investment Advisers medium term views on key market drivers; for example, technology via US technology, or a single country via India. Investors in the Fund should have a minimum investment horizon of at least five years. Over shorter</p>

		<p>time periods there is the risk of a loss in investment capital.</p>
<p>What are the inherent risks imbedded in the Fund?</p>	<p>The principal risks of investing in the Fund are risks relating to:</p> <ul style="list-style-type: none"> <li>• investing in shares;</li> <li>• the investment objectives not being met;</li> <li>• the performance of a particular company they have invested in;</li> <li>• the concentration of the Fund in a particular region, industry, or other grouping;</li> <li>• Unit pricing or taxation errors; and</li> <li>• currency risk management between the New Zealand dollar and global currencies.</li> </ul>	<p>The Manager and the Investment Adviser are aware of a broad range of risk embedded in the Fund. These have been detailed in the Managers response to the question.</p> <p>The relationship between the Manager and Investment Adviser is collaborative, with the Investment Adviser providing thematic ideas and ways in which the Manager can implement each thematic. The Manager is ultimately responsible, and has discretion to veto recommendations from the Investment Adviser. Any decision acted on, or vetoed, may influence future performance or risk characteristics.</p> <p>To assist in managing risk, the Investment Adviser has embedded ETF selection, tracking errors, country, sector and currency exposure limits in to its portfolio and management process. Similarly, the Manager, via its operations and compliance teams, ensures that portfolio guidelines are not breached.</p>
<p>Why does the Manager believe the future prices of the Fund's investments will vary?</p>	<p>The Manager has appointed JBWere as the Investment Adviser, to develop and implement the themes and how to implement the themes in the portfolio. Devon is ultimately accountable for the Fund and retains the right to veto Investment Adviser recommendations.</p> <p>The Manager believes that relatively broad themes can be readily identified and invested in using ETFs and index funds predominantly. The Manager has appointed the Investment Adviser to assist in identifying themes, and ways to invest in them</p>	<p>FundSource views the Fund's approach to constructing this portfolio positively. The Manager recognises where its core strengths lie, and has appointed an Investment Adviser to identify a series of global themes, incorporating macro data to determine the markets and types of instruments available to gain investment exposure.</p> <p>The Investment Adviser conducts its own research around ETFs and index funds, enabling it to accurately reflect its thematic views. This includes utilising the research provided by external sources such as sell side brokers and independent research providers.</p> <p>The Investment Adviser uses a logical framework, to determine which part of the cycle a theme is in. The Investment Adviser breaks the cycle in to three parts, the controversial, realisation and consensus phases. While the Investment Adviser is not looking to time the market, understanding at which phase a theme sits in is important, as it dictates if the Investment Adviser will recommend investing in, or selling out of a theme. The Investment Adviser looks to identify a theme early to develop their internal view. This will typically see a recommendation before or soon after a theme has gained some traction, generally toward the bottom of the realisation phase. The Investment Adviser looks to advise selling a theme around the time the market is forming a consensus view.</p> <p>The Manager reviews the themes and execution strategy provided by the Investment Adviser. The Manager is under no obligation to accept all Investment</p>

		Adviser recommendations. The Manager regularly discusses the Fund with JBWere, the Investment Advisers.
Why does the Manager believe you should give them your money rather than to someone else or to an inexpensive index fund?	The Manager clearly articulates its <a href="#">investment philosophy</a> and process, which it has been adhering to since the inception of the Fund.	<p>The Fund's return to investors, available on the <a href="#">Manager</a> and the <a href="#">Disclose</a> website, highlights the Funds return compared to the Funds benchmark, the i-Shares MSCI All Country World index exchange traded fund, 50% hedged to New Zealand dollars.</p> <p>The Manager has three core statements which are publicly available through the Managers <a href="#">values and client care statements</a> and approach to <a href="#">responsible investment</a>. These statements clearly spell out the commitment Devon undertakes to investors and how they manage funds on behalf of investors. The statements published on Devon's website do differentiate the Manager, in that few managers clearly articulate this in writing.</p> <p>In conjunction with a disciplined approach to investing, the Manager, presents a clear rationale as to why a potential investor should consider investing in this Fund.</p>
How does the Manager decide to buy or sell investments?	<p>The Investment Advisers recommendations are based on their assessment of a particular theme's positioning in its investment cycle. Ideally themes are build up in the "controversial" or "realisation" phase and sold in the "consensus" phase, when the theme's potential has become widely recognised by the market. The adviser uses a range of quantitative and qualitative tools to make this assessment.</p> <p>The Manager has appointed JBWere as the Investment Adviser. Devon is ultimately accountable for the Fund and retains the right to veto Investment Adviser recommendations.</p>	<p>FundSource believes that the Investment Adviser's critical insights are focused on the determining the commencement and ending of the realisation phase, rather than trying to enter too early and sell too late. This mitigates timing the market, as the Investment Adviser is prepared to wait before recommending a theme. Likewise, the Investment Adviser is prepared to take profits and exit a theme, rather than continue to remain invested, and risk a loss of capital.</p> <p>The key differentiator, compared to other Devon funds is the appointment of an Investment Adviser, introducing counter party risk, largely mitigated by the Manager retaining the right of veto over the Investment Adviser recommendations.</p> <p>The Manager, in approving themes and the method to implement, typically takes a long-term view.</p> <p>All investment ideas and portfolio changes are reviewed by Devon's Investment Committee (which currently includes the entire investment team, the Managing Director and a representative from the Compliance team).</p>
Has the CIO/ Portfolio Manager personally invested in the Fund? If so, paying the same fees as other investors?	The investment staff and senior managers are investors in the Devon Funds and on the same terms as all other investors. The JBWere Investment team are also investors in the Fund on the same terms as other investors.	<p>FundSource believes that the interests of investment personnel are better aligned to those of the investors, when investment personnel are significantly invested, at the same fees.</p> <p>Effectively, the investment team are eating their own cooking, bringing strong investor alignment.</p>
How much latitude does the Manager have to deviate from the weightings of the Benchmark portfolio?	The Portfolio Manager has complete discretion as to which stocks and fixed	Individual global security positions can have a significant impact on the overall return of the portfolio, especially over

	<p>interest securities are used to build the portfolio.</p> <p>Tracking Error (5 yr): 5.91  Cash Allocation: 0%-20%  Global Financial Assets: 80%-100%  Single Stock Limit: Not Specified  Sector Limits: None  Currency Hedging: 0%-100%</p>	<p>shorter time periods, say, one year. FundSource views that the Portfolio Manager's level of discretion is expected to result in the return of the Fund differing significantly from that of the performance benchmark. Investors seeking a benchmark-like return may not be suited to the Fund.</p> <p>Most constraints are soft, providing further latitude for the manager to implement the process. This is reflected in the Manager's approach to hedging, where investors should expect the Fund to be typically hedged at 50%, but the Manager can hedge from 0-100%.</p>
<p>On what basis does the Manager believe the fees they charge are justified?</p>	<p>The manager charges a base fee of 0.90% p.a. plus GST.</p>	<p>The Manager's basic fee is well below the average fee charged by peer funds in the FE Analytics NZMI Equity Global sector. FundSource notes this remains the case with the Funds administration fees added.</p>
<p>How would you describe the quality of your organisational and investment governance processes?</p>	<p>The Manager's board consists of six directors, four of whom are independent. The Audit, Risk &amp; Compliance Committee and Remuneration Committee are chaired by one of the Independent Directors.</p> <p>The Managing Director heads the Operations Team, totalling seven staff. The Supervisor, Custodian, and Registrar/Administration functions are outsourced to reputable firms.</p>	<p>The Manager has a strong governance structure which starts with the composition of the Board and leadership of key Board Committees. In addition to the out-sourced functions, there are sufficient internal personnel in operational roles, to ensure that the four investment team members can concentrate on managing the portfolios.</p> <p>The integration of the environment, social and governance (ESG) policies in to the research process is viewed positively. The important aspect that underpins UNPRI and ESG is the application of the principles, with active ownership being one factor Devon specifically state in their approach to <a href="#">responsible investing</a>.</p>
<p>Is there alignment of interests through; ownership of the Manager, and remuneration of the investment team?</p>	<p>The Manager, Devon Funds Management Limited, is a 100% subsidiary of the Investment Services Group Limited which is wholly owned by interests associated with the staff and directors. Devon was established in March 2010 when it acquired the asset management business of Goldman Sachs JBWere NZ Limited.</p> <p>Staff salaries are slightly below market by design. Compensation also comes from the bonus pool and is directly tied to the performance of funds/portfolios and the business. A number of funds/portfolios have performance fees so that the firm and client incentives are aligned. However, the Global Themes Fund does not have a performance fee at this time.</p>	<p>Being 100% owned by its employees and directors, there is strong buy-in from the team to work hard for the firm's long-term success - this is good news for investors.</p> <p>There is alignment between the bonus component of staff remuneration and the performance of the funds/portfolios, although FundSource doesn't know how bonuses are calculated and thus can't comment on the extent to which it is aligned to the interests of investors.</p>

## Conclusion and Rating

The Fund provides exposure to a global equity portfolio that predominantly uses ETF's and index funds to execute its strategy, making this a differentiated proposition compared to other global equity retail options in New Zealand. The Investment Adviser can use highly targeted sector, country and regional ETF's or index funds. Therefore, the actual portfolio can bear little resemblance to its benchmark. Individual company exposure is not considered a significant risk, as the use of ETF's and indices will bring security diversification to the portfolio. Ultimately the Manager, Devon, is responsible and accountable for the Fund, despite leveraging JBWere.

The Fund uses passive investment vehicles; however, this does not preclude the Fund from investing via direct securities. Importantly Investors should not perceive this Fund as being a passive fund, or confuse this fund as replicating a broad global equity index, or using broad equity indices to implement the strategy. The Fund is actively managed and will transition across broad themes through the market cycle.

FundSource believes the appointment of an investment adviser to the portfolio is a positive move, reflecting the Manager's internal focus on Australasian equities. Understanding core skills,

and determining an appropriate way to access skills, when required, is reflective of a Manager who has strong knowledge and conviction in their investment operations. The appointment of JBWere as the investment adviser is viewed positively, and is aligned with FundSource's conviction in the Manager. This is underpinned by the Manager's measured approach to growing the investment team over time, methodical research process, which includes oversight from the Investment Committee, and the ability to attract staff.

The Manager's basic fee is well below the peer average in the FE Analytics NZMI Equity Global sector.

FundSource recommends that investors carefully consider that the Managers active ETF and index based approach to investing in global equity markets meets their investment needs and objectives.

### FundSource Rating: **AA**

Fund ratings are current as at the date of publication of this report. FundSource reserve the right to review and update fund ratings from time to time.

## Research Factor Weighting

Research Process Category	Model Factor Weight	Analyst Average Score
Corporate & Investment Governance	15%	4.25 / 5
Investment Philosophy & Process	20%	4.40 / 5
People	25%	4.00 / 5
Portfolio Construction & Implementation	15%	3.50 / 5
Risk Management	15%	3.80 / 5
Investment Fees	10%	3.71 / 5

**Overall Average Score: 3.98 / 5**

## FundSource Rating Guide

The qualitative rating of a fund is a function of the FundSource Research Factor Weighting process, which is built around the six core qualitative research process categories. The weighted scores result in an overall score, out of five, which is then matched to the following rating:



### AAA: Highly Recommended

Funds that have superior average scores in all six underlying qualitative factors. This recognises aspects about the Manager and Fund in question that includes, but is not limited to, significantly experienced and stable senior personnel, a sound track record over a full market cycle, a clearly defined investment philosophy and process, and a portfolio consistent with that philosophy and process. The management company will also have established effective controls to maintain that philosophy.

### AA: Recommended

Funds that have strong average scores in all six underlying qualitative factors. This recognises aspects about the Manager and Fund in question that includes, but is not limited to, experienced and stable personnel, a sound track record over a full market cycle, a clearly defined investment philosophy and process, and a portfolio consistent with that philosophy and process. The management philosophy must be coherent and consistent with existing portfolios and processes.

### A: Investment Grade

Funds that have good average scores in all six underlying qualitative factors. This recognises aspects about the Manager and Fund in question that includes, but is not limited to, experienced personnel, a sound track record a defined investment philosophy and process, and a portfolio consistent with that philosophy and process.

### FW: Fund Watch

There has been a material change with either the manager, this may include, but is not limited to, departures, new hires, process changes, changes to the investment philosophy. This is considered to be an interim measure, to enable further investigation, re-evaluation and an appropriate course of action to be determined.

### S: Sell

This category covers previously recommended funds that are no longer recommended because of some material change. Removal from recommended status might be for a variety of reasons such as a fundamental change in the fund management company or in the manager's investment strategy, or because a fund did not meet its original expectations. The implications for ongoing service are that the fund should be reviewed on an individual client basis to ensure it still matches their original investment objective.

### NR: Not Rated – Screened/ Not Rated

Funds in the Not Rated – Screened category have provided information and/or FundSource has conducted an initial analysis of the fund, but has chosen not to provide a recommendation at this stage. FOR Not Rated funds the manager may have provided information, but no review meeting has been conducted

## Disclaimers, Disclosures and Warnings

**FundSource Limited notes that the information in this report must be read in conjunction with the warning and disclaimer below. This report supersedes all prior reports.**

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By leveraging the skills of specialists, Research IP is able to provide innovative and tailored financial services solutions to the market place. Client focused outcomes are underpinned by the belief that the role of business model innovation and accelerating technological change opens up new possibilities, to put client interests at the centre of the financial services industry focus, based on John Hagel's work on the possibilities for "Disruption by Trusted Advisors" and John Kay's "Other People's Money: Masters of the Universe or Servants of the People".