



FOR THE USE OF AUTHORIZED FINANCIAL ADVISERS OR WHOLESALE CLIENTS ONLY

1) *"Our models show both the S&P 500 and the S&P/TSX in 'fair-value' range."*

Andrew Adams CFA, Raymond James' *Investment Strategy*, March 22nd, 2018

2) • *"I did not intend to get rich, I wanted to get independent. I just overshot ..."*

- *"The people that have outcomes that seem extraordinary are the people who have discipline, and intelligence, and good virtue plus a hell of a lot of luck."*

Charlie Munger, Berkshire Hathaway, addressing U. of Michigan, Bus School Grads 2017, on 'How to Succeed at Life'.

QUARTER COMMENCING July, 2018

Norman Stacey, Investment Strategist

Diversified Investment Management Services Ltd

Key to Strategy process is responding to anticipated macroeconomic developments. Strategies attempt to position portfolios ahead of likely events in one-year to 18-months. Shorter-term decisions and trading opportunities are generally delegated to the active managers selected. In operating a one-year to 18-month horizon particularly for macro-economic parameters strategies are formally reviewed quarterly.

SUMMARY

- 1 The pace of the synchronous global economic expansion is levelling off. Modest increases among laggard Emerging Markets, offset slight tapering of pace by erstwhile leaders. But growth it is – at a still robust aggregate pace, and above-trend pace in many places.
- 2 Output gaps have closed or are closing. Rising commodity prices – including energy – and labour cost pressures are fueling inflation. Populist politics also tend to be inflationary. Inflation risks may be underestimated.
- 3 In the USA, monetary policy is projected to progress through ‘neutral’ toward restrictive over the coming 18 months – even as fiscal policy loosens.
- 4 The progressive unwinding of QE in USA, and cessation of QE in Europe creates headwinds for some Emerging Markets.
- 5 Revision of US trade policy may be warranted but the methodology is generating uncertainty for all. This unsettles the broad, synchronous, global growth cycle underway – but may also serve to slow and thereby extend it.
- 6 China’s growth is projected to cool only slightly, and it continues to display adept economic management. Monetary stimuli are fading, trade imbalances are narrowing, while once-heady credit growth is moderating.
- 7 Our best research sources counsel remaining engaged in growth assets for now.
- 8 From current valuations, risk in financial markets is elevated. Bonds are very expensive; Property & Infrastructure are highly-priced, leverage is extended, and broad Equity indices travel at high levels. Looking ahead, the immense monetary stimuli that fuelled these ‘bull-market’ years is being relentlessly withdrawn.
- 9 We recognise the multi-century downtrend in Commodity prices, but also that periodic strong rallies make worthy cyclical investments. Amidst generally stretched valuations, commodity-producers’ valuations present as comparatively attractive. Irrespective of the bounce since Feb. 2016, we gauge the rally has further to run. A tactical allocation to this asset class is advocated.
- 10 In the expected absence of further broad market advances, decent portfolio returns ahead will be reliant on proprietary talent and manager skill. The Long and Short Equity style, at least theoretically, has scope to exploit either under- or over-priced anomalies. The ‘short’ component should also provide some structural resilience in the event of downside market volatility.
- 11 Fundamentally, portfolio returns of recent years have been unusually high. These recent levels are most unlikely to be sustained over the investment cycle.
- 12 But for now, strategies remain significantly engaged in selected growth assets. With history as a guide, some of the best investment gains have been achieved toward the end phases of broad economic expansions. Our aim to capture a portion of the late-stage rallies anticipated.

TABLE OF CONTENTS

SUMMARY	2
TABLE OF CONTENTS.....	3
I) MACROECONOMIC SETTING.....	3
Global Economic backdrop – from Published Data	3
Overview of World Economic Outlook - Projections	4
Global monetary & Fiscal policy settings are trading places	5
Inflation: destined to Rise - the ‘slack’ has been taken up	5
USA – GDP growth May be peaking	6
China – disappearing Current aCCOUNT SURPLUS.....	8
Europe – Germany has a financial Problem (& it is not Greece)	9
Emerging & Frontier Economies – A house divided.....	9
Australasian Economies – Middling Growth; macro variances	11
Summary – What’s ‘in-the-Market’?	12
Global Macroeconomic Risks – Interpretation & Analysis.....	12
II) SALIENT ECONOMIC INFLUENCES ON ASSET CLASSES & FINANCIAL MARKETS.....	13
Administered Rates & Bonds – Easy Money is waning	13
Equities – not as stretched as some commentators decry.....	16
Commodities – the favoured tactical asset class currently	17
Portfolio Strategy Risks / Vulnerabilities	20
III) STRATEGY – ASSET SECTOR RESPONSES.....	20
Summary of Asset allocation Changes Resulting from Review.....	21
Comparative Asset Allocation - <i>Diversified’s</i> Reference AA with NZ Industry.....	21
VI) <i>DIVERSIFIED’S</i> INDICATIVE INVESTMENT PORTFOLIOS – JULY 2018.....	22

I) MACROECONOMIC SETTING

GLOBAL ECONOMIC BACKDROP – FROM PUBLISHED DATA

Global economic forecasts remain bullish. The robust, and above-trend growth pace attained in 2017 is persisting in 2018 and is projected to taper only very marginally within our tactical horizon.

Slightly lesser but still robust projected growth from the Developed World & China ahead, is expected to be largely offset by increased growth across South America.

Scenarios similar to the projections summarized below are very widely held, and therefore deemed to be substantially in-the-market.

OVERVIEW OF WORLD ECONOMIC OUTLOOK - PROJECTIONS

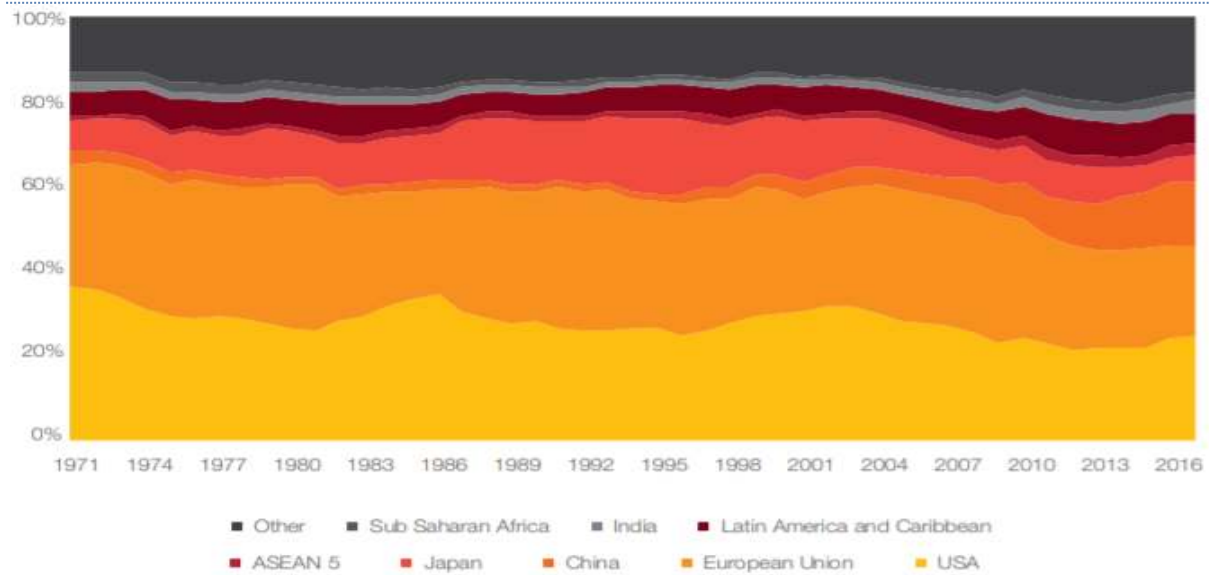
International	2000-16	2016	2017	2018f	2019f	2000-16	2016	2017	2018f	2019f
	Real GDP (annual % change)					Consumer Prices (y/y % change, year-end)				
World (based on purchasing power parity)	3.9	3.2	3.8	3.8	3.7					
Canada	2.1	1.4	3.0	2.2	2.1	1.9	1.4	1.8	2.4	2.3
United States	1.9	1.5	2.3	2.6	2.4	2.2	1.8	2.1	2.4	2.4
Mexico	2.2	2.9	2.0	2.3	2.8	4.4	3.4	6.8	4.1	3.8
United Kingdom	1.8	1.9	1.8	1.7	1.9	2.0	1.6	3.0	1.9	1.9
Eurozone	1.3	1.8	2.5	2.5	2.3	1.7	1.1	1.4	1.5	1.5
Germany	1.3	1.9	2.6	3.0	3.0	1.5	1.7	1.6	1.6	1.9
France	1.3	1.2	1.9	2.5	2.0	1.6	0.8	1.2	1.5	1.5
China	9.4	6.7	6.9	6.5	6.2	2.3	2.1	1.8	2.3	2.5
India	7.1	7.9	6.4	7.4	7.5	6.9	3.4	5.2	4.6	5.6
Japan	0.9	0.9	1.7	1.3	0.9	0.1	0.3	1.0	1.1	2.3
South Korea	4.2	2.9	3.1	2.8	2.8	2.6	1.3	1.5	2.1	2.5
Australia	3.0	2.6	2.3	2.6	2.5	2.8	1.5	1.9	2.2	2.6
Thailand	4.0	3.3	3.9	3.5	3.4	2.0	1.1	0.8	1.0	2.0
Brazil	2.6	-3.5	1.0	2.5	2.7	6.7	6.3	2.9	4.1	4.6
Colombia	4.1	2.1	1.8	2.5	3.5	5.1	5.7	4.1	3.3	3.4
Peru	5.1	3.9	2.5	3.3	3.7	2.8	3.2	1.4	2.0	2.5
Chile	4.0	1.2	1.5	3.6	3.9	3.4	2.7	2.3	2.7	3.0
Commodities										
	(annual average)									
WTI Oil (USD/bbl)	63	43	51	65	68					
Brent Oil (USD/bbl)	66	45	55	70	73					
WCS - WTI Discount* (USD/bbl)	-17	-14	-13	-22	-20					
Nymex Natural Gas (USD/mmbtu)	4.94	2.55	3.02	2.80	2.85					
Copper (USD/lb)	2.35	2.21	2.80	3.10	3.25					
Zinc (USD/lb)	0.81	0.95	1.31	1.60	1.60					
Nickel (USD/lb)	7.25	4.36	4.72	6.00	6.50					
Aluminium (USD/lb)	0.88	0.73	0.89	0.95	1.00					
Iron Ore (USD/tonne)	67	58	72	63	80					
Metallurgical Coal (USD/tonne)	127	114	187	162	160					
Gold, London PM Fix (USD/oz)	869	1,251	1,257	1,310	1,300					
* 2008-16 average										
Sources: Scotiabank Economics, Statista Canada, BEA, BLS, IMF, Bloomberg										

Source: Scotiabank's Forecast Tables, May 3rd, 2018

Broad, synchronous economic growth it is, at substantially the same robust aggregate pace throughout the year to 18 months of our tactical horizon.

China's economic rise over the past two decades - indeed an 'economic miracle' - is projected to persist. But fortunately, neither China nor any single region, is the dominant factor in the rosy expectation for global growth.

ITS NOT ALL ABOUT CHINA (OR USA, OR EUROZONE) – PERCENTAGES OF GLOBAL GDP

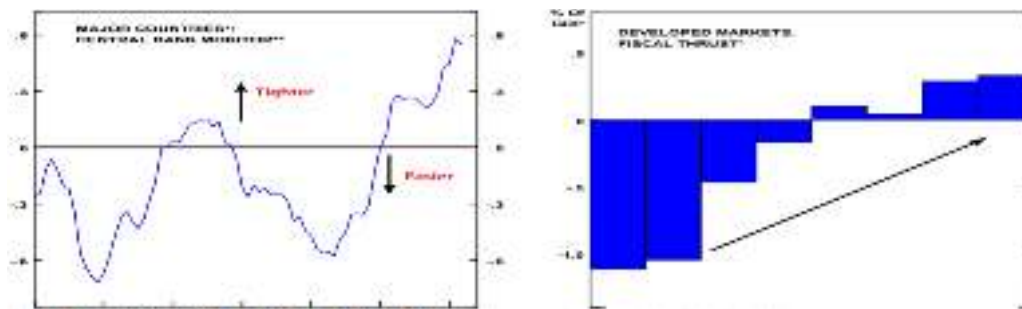


Source: PwC Analysis, May, 2018

GLOBAL MONETARY & FISCAL POLICY SETTINGS ARE TRADING PLACES

Just as Monetary policy settings are on a trajectory from stimulatory, through normalising and toward restrictive, (Quantitative easing is being unwound, and administered rates should near 'neutral' in flagship USA in 2018/2019), so austerity fatigue, tax-cuts & populist government policies are turning Fiscal policy stimulatory.

MONETARY POLICY VS FISCAL POLICY - DEVELOPED COUNTRIES

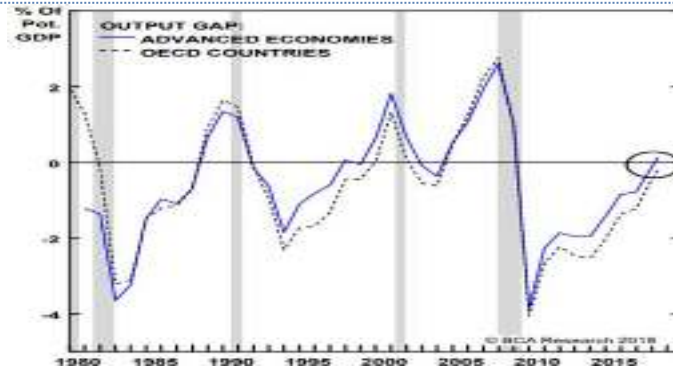


Source: BCA Research, 'Anticipating the Turn' presentation Chartpack, May 2018

INFLATION: DESTINED TO RISE - THE 'SLACK' HAS BEEN TAKEN UP

The aggregate global output gap – surplus capacity in national economies available to meet greater demand – that had prevailed post-GFC, has now mostly closed. Sustained growth at a pace near that recently will henceforth stimulate inflation.

THE GLOBAL OUTPUT GAP HAS CLOSED



Source: BCA Research, 'Anticipating the Turn' presentation, May 2018

Key Points:

Synchronous, robust global growth is expected throughout our tactical horizon;

Mildly tapering paces of growth in Developed Economies & China in 2019, is likely to be countered by quickening paces in elsewhere;

But it is late in the current global economic expansionary cycle, when inflationary pressures traditionally build;

The extreme, monetary stimulus post GFC is normalizing, and;

Continuing global economic prosperity is the current assumption in financial analyses and broad market valuations.

USA – GDP GROWTH MAY BE PEAKING

Following a slightly softer Q1, US economic growth is projected to record 3%+ in Q2 & Q3 as tax cuts apply. Beyond that, the pace may cool a little in 2019 and 2020 as Administered Interest Rates are normalized.

IMPRESSIVE NEAR-TERM GROWTH MAY BE AS-GOOD-AS-IT-GETS

	4Q'17a	1Q'18a	2Q'18f	3Q'18f	4Q'18f	1Q'19f	2Q'19f	3Q'19f	2017a	2018f	2019f
Real GDP (Percent Change Annualized)	2.9	2.2	3.6	2.8	2.8	2.5	2.5	2.5	2.3	2.9	2.6
CPI (Percent Change Year-over-Year)	2.1	2.3	3.0	3.2	3.1	2.8	2.5	2.2	2.1	2.9	2.4
Payroll Jobs (Average Monthly Diff., Ths.)	185.4	210.8	194.7	176.2	165.7	149.3	146.0	139.9	181.4	186.8	142.7
Unemployment Rate (Percent)	4.1	4.1	3.9	3.8	3.8	3.7	3.7	3.7	4.3	3.9	3.7
Federal Funds Rate (Effective)	1.20	1.45	1.71	1.91	2.13	2.17	2.42	2.66	1.00	1.80	2.53
10-Yr. Treasury Rate	2.37	2.76	2.93	3.05	3.18	3.16	3.37	3.59	2.33	2.98	3.48

Source: Comerica Bank, US Economic Outlook, June, 2018

Unemployment is now at a level which has historically stimulated wage growth. A fourth Fed Funds rate-hike is now widely anticipated in the 2018 calendar year (Dec), with steady increases throughout 2019.

Tax-cuts are invariably inflationary.

Consumer Inflation in flagship USA is gathering pace.

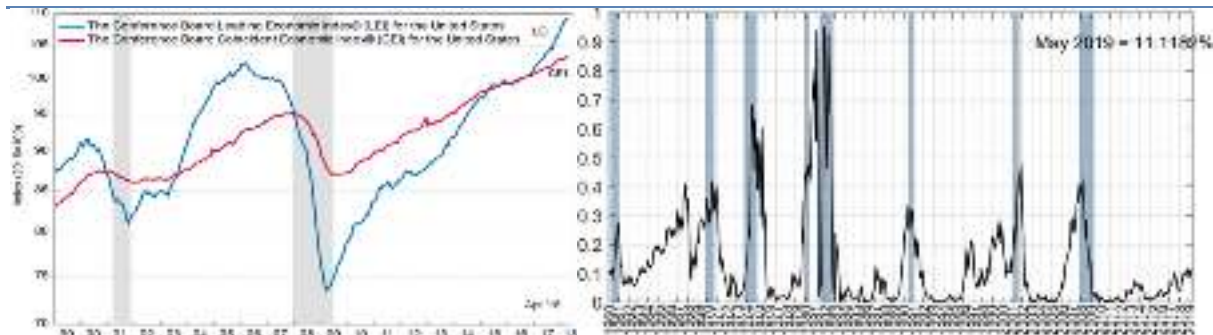
USA INFLATION INDICATORS



Source: Comerica Bank, US Economic Outlook, June, 2018

Meanwhile, US Leading Economic Indices provide comfort that no downturn is likely in 2018 – neither is it likely to accelerate strongly. Further, the ‘probability-of-recession-in-the-next-12-months’, as might be signalled if the widely-respected and historically predictive yield curve inverted (10-yr rate minus 3-month T-Bill), is comfortingly low.

US LEADING ECONOMIC INDEX SUPPORTIVE ... & PROBABILITY OF RECESSION VERY LOW



Source: The Conference Board's L. E. Index, May 17th, 2018

Source: NY Fed, updated to June 4th, 2018

TRADE WARS /SKIRMISH - TRUMP HAS A POINT

President Trump has raised hackles with his unilateral tariff hikes, and assertion that USA's trading partners have taken advantage of USA. [*"We're like the Piggy-bank that everybody is robbing"*. President Trump at G7 meeting in Quebec, 10th July, 2018].

Country / Region	Average Tariff
China	9.9%
Mexico	7.0%
European Union	5.2%
Canada	4.1%
Japan	4.0%
USA	3.5%
Australia	2.5%
NZ	2.0%

Source: WTO/ UNCTAD, World Tariff Profiles, 2017, 'Simple Average MFN Duty'.

The USA has been subject to many years of unfair trade practices by the Europeans, Japanese & Chinese, through asymmetric tariffs or restrictions. (e.g. Canada's almost total protection of its Dairy industry – average 249% tariff on imports - & managed to get it ability to continue that into the TPPA)

Key Points:

Expectations are that USA growth will continue at a slightly lesser, but still robust pace;

Inflation is rising. Risks are to the upside;

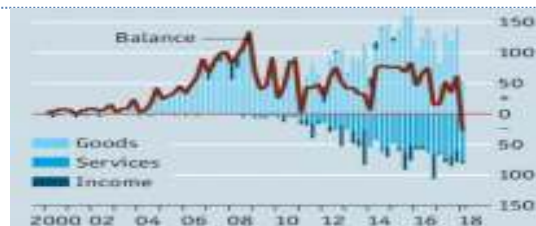
Tariffs are still excessive around the world, and;

Led by the USA, a rising Administered Interest Rate cycle is underway.

CHINA – DISAPPEARING CURRENT ACCOUNT SURPLUS

Chinese tourists travelling abroad have created a burgeoning trade deficit in Services (about matching and therefore offsetting its legendary surplus in export of Goods). The demise of China's once provocative Current Account Deficit fosters the Yuan's progression as an international currency, albeit likely with greater, short-term exchange rate fluctuations ahead.

CHINA'S CURRENT ACCOUNT, US\$ BILLION



Source: The Economist, May 19th, 2018

Superficially, China has a substantial Debt issue; Total Debt is approaching 250% of GDP – mostly loaned to corporate & SOE borrowers. To a significant extent, Debt in China reflects the low development of its Equity markets. Chinese are prodigious savers, and Debt is necessary to recycle the saving glut into the economy.

CHINA'S SAVINGS PROBLEM



Source: BCA Research, 'Anticipating the Turn' presentation, May 2018

Key Points:

China's economic growth may ease slightly, but to a still robust pace and off a higher base;

With its place in the economic world established, recognition as a super-power is progressing & inevitable;

Some contentious imbalances are being addressed, notably its Current Account Surplus, and recycling of Household Savings;

China's economic success & management serve as exemplar for Emerging Economies more broadly, and;

Continued strong end-user demand in China underpins real demand for Commodities.

EUROPE – GERMANY HAS A FINANCIAL PROBLEM (& IT IS NOT GREECE)

Germany is Eurozone's banker; it has a credit problem. This Creditor has extended a cumulative €900 billion credit (trade imbalance) to the rest of Euroland; with Spain and Italy the dominant Debtors. Both have deteriorating creditworthiness: Spain is wrestling with break-up (Catalonia & maybe Basque regions). Meanwhile, Italy has just elected a Eurosceptic government, with some factions angling to leave the bloc.

EURO-SYSTEM TARGET2 BALANCES



Source: Gold Monitor, Murenbeeld & Co, June 1st, 2018

While Eurozone's growth projections continue to be robust, internal trade imbalances leave the region increasingly reliant on external demand to fuel that growth. The bloc is consequently especially vulnerable should global to trade skirmishes intensify.

Key Points:

Projected Eurozone GDP is 'good' by European standards;

QE is no longer required (should cease this year);

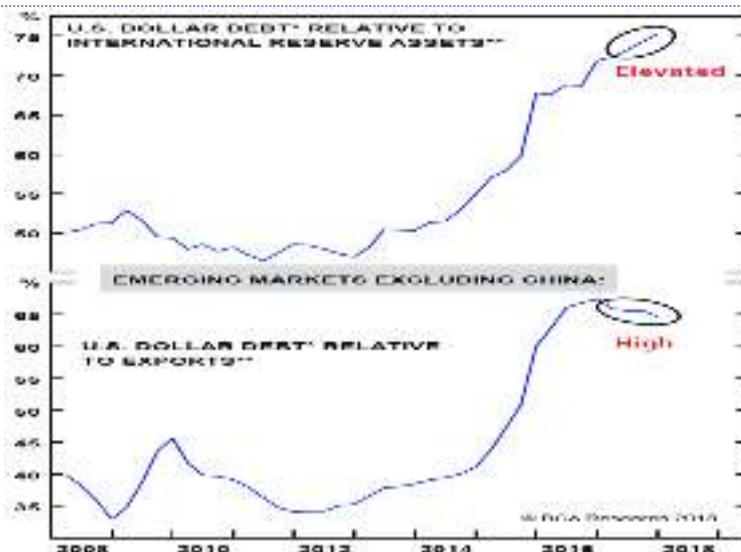
Euro stability & prosperity is reliant on German largesse, and;

Eurozone's prosperity is vulnerable in the unlikely event a 'Trade War' develops.

EMERGING & FRONTIER ECONOMIES – A HOUSE DIVIDED

Selected, steep rise in Debt levels, and especially foreign denominated (mostly US\$) Debt issuance over the past couple of years, detracts from Emerging Markets' erstwhile comparatively sound national accounts.

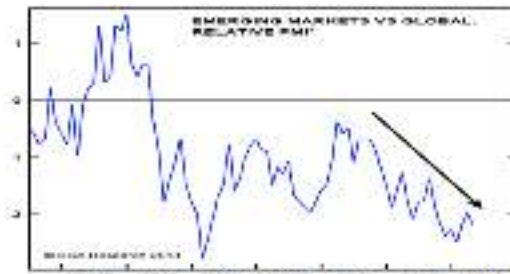
STEEPLY RISING DEBT OBLIGATIONS



Source: BCA Research, 'Anticipating the Turn' presentation, May 2018

And higher EM debt levels - in aggregate; not everywhere - are not necessarily reflected in proportionately higher growth; quite the inverse. EM economies reliant on IT & manufacturing may be depressing the average, while growth among primary producers (e.g. South America) and Oil exporters is lifting.

AGGREGATE EM GROWTH OFF THE BOIL – PURCHASING MANAGER’S INDEX



Source: BCA Research, 'Anticipating the Turn' presentation, May 2018

We anticipate growth among Emerging Economies to diverge, with those producing primary resources, energy and materials being more prosperous.

Emerging Markets – favored ones supply what China needs

IMPORT ITEMS	% OF TOTAL IMPORT VALUE
MATERIALS (METALS, CHEMICALS AND OTHER CRUDE MATERIALS)	26.0%
INDUSTRIAL MACHINERY	27.6%
ENERGY (COAL, OIL, GAS AND ELECTRICITY)	12.0%
OTHER MANUFACTURED GOODS	9.0%
OFFICE MACHINES AND TELECOM EQUIPMENT	6.9%
ROAD VEHICLE AND OTHER TRANSPORT EQUIPMENT	6.0%
PROFESSIONAL INSTRUMENTS AND WATCHES	5.5%
FARMING AND ANIMAL PRODUCTS	3.5%
TOTAL	100.0%

Source: BCA Research, 'Anticipating the Turn' presentation, May 2018

In the longer-term, superior growth rates and demographics suggest at least selected Emerging Economies will continue to gather increasing prominence in the global Economy over coming decades.

Key Points:

Emerging & Frontier Economies are for convenience treated as an aggregate for asset allocation purposes, despite significant differences in underlying economies;

Primary Resource producers are favoured over manufacturers for our tactical horizon.

AUSTRALASIAN ECONOMIES – MIDLING GROWTH; MACRO VARIANCES

AUSTRALIA – SUNNY FORECAST IS BACK

An enviable pace of growth ahead looks set to restore Australia's status as the 'lucky country' amongst the Developed World.

FORECAST - KEY AUSTRALIAN ECONOMIC PARAMETERS

	Dec 2017	Jun 2018	Dec 2018	Jun 2019	Dec 2019	Jun 2020
GDP growth	2.4	2%	3%	3½	3%	3
Unemployment rate ⁽¹⁾	5.3	5½	5½	5%	5%	5%
CPI inflation	1.9	2	2½	2½	2½	2½
Underlying inflation	1.4%	2	2	2	2	2½

Source: RBA, Statement of Monetary Policy, May, 2018

NEW ZEALAND – THE OFFICIAL OUTLOOK IS ROSY

NZ's May 17th Budget forecasts growth accelerating through to 2020, while inflation remains at less than the mid-point of the RBNZ's mandated band. The forecasts will be convenient for government if achieved. It appears ambitious.

NZ ECONOMIC PROJECTIONS – ANNUAL YEARS TO JUNE 30TH

June years	2017	2018	2019	2020	2021	2022
	Actual	Forecast	Forecast	Forecast	Forecast	Forecast
Economic						
Real GDP (production basis, annual average % change)	3.3	2.8	3.3	3.4	2.7	2.5
Real GDP per capita (production basis, annual average % change)	1.2	0.7	1.3	1.7	1.3	1.3
Unemployment rate (annual average, %)	5.0	4.5	4.4	4.1	4.1	4.2
CPI inflation (annual average % change)	1.4	1.5	1.4	1.7	1.9	2.0

Source: NZ Treasury, Budget Economic and Fiscal Update, May 17th, 2018

Key Points:

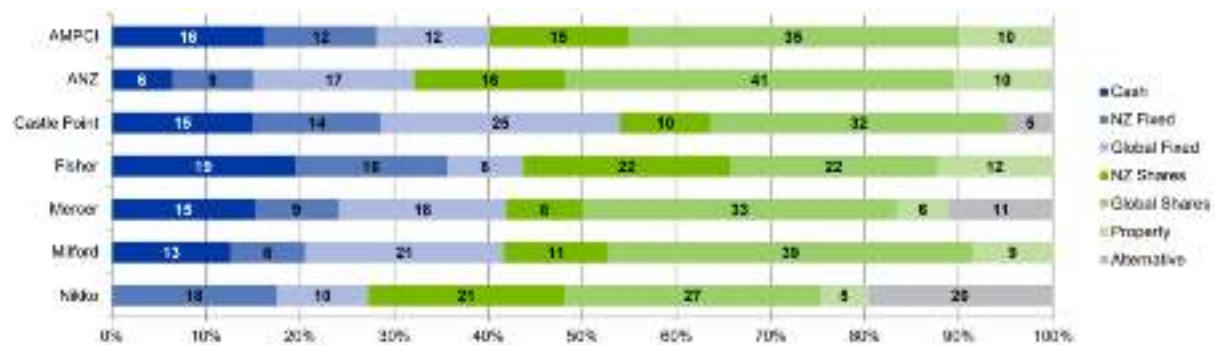
- 1) *Robust growth accelerating into 2019/20 officially expected by both Australian & NZ gov'ts, may be more credible for Australia;*
- 2) *The rosy official expectations severely restrict scope for upside surprises in growth;*

- 3) *Australian inflation is projected to be higher than the sedate pace forecast for NZ, suggesting Australia's OCR may move up sooner, and;*
- 4) *The Economic backdrop suggests solid corporate earnings reigning in both nations throughout our tactical horizon.*

SUMMARY – WHAT'S 'IN-THE-MARKET'?

As a proxy for what is 'in-the-markets', the asset allocations for 'Balanced' investment profiles of seven institutional investment houses is provided.

INSTITUTIONAL ASSET ALLOCATIONS



Source: The AON Investment Update as at 30th April, 2018.

Key Points:

- 1) *Institutions apparent expect Global Equities to be the best performing asset class (32.7% allocation), followed by Global Fixed Interest (15.8%), and NZ Shares (14.7%).*
- 2) *Relatively low Cash allocations suggest concerns over Financial Market valuations are at a low ebb among Instos;*

GLOBAL MACROECONOMIC RISKS – INTERPRETATION & ANALYSIS

The official & widely-held view – shared by governments, parastatals or institutions – is that a benign global setting with above-trend growth and tame inflation will persist. This setting will allow easy financial conditions persisting globally for the next couple of years.

The central scenario, is that US administered rates will be only gradually raised, not achieving net 'tight' settings for some years.

From this very rosy expectation, macroeconomic risks must be regarded as being asymmetrical to upset – if growth disappoints; inflation exceeds low expectations, or more vigorous Official Cash Rates hikes result.

INFLATION RISK – HIGH PROBABILITY OF ‘SURPRISE’ TO THE UPSIDE

Inflation had been suppressed by an Output Gap which has now substantially closed. The current global economic expansion is one of the lengthier on record, with Inflationary pressures tending to build in late-cycle. Long suppressed wage pressures have palpably returned. Tax cuts are always and everywhere inflationary. The deflationary offset in recent years - from falling commodity prices, and cheaper Chinese imports - has ceased and reversed.

Headline rates of inflation across major countries rising since 2016, are officially interpreted as a blip, soon to taper. We gauge that rise more likely the initial stages of a sustained rally.

The risk of inflation being higher than is a consensus – or is in-the-market – is considerable.

ECONOMIC RESILIENCE AMIDST MONETARY HEADWINDS

USA administered rates are on an upward trajectory. The USA’s Federal Reserve Board forecasts its Fed Funds Rate could achieve a ‘neutral’ level (*circa* 2.7%) in 2019 – beyond which unexpected ‘tight’ settings will proceed. Simultaneously, the Federal Reserve Board’s, Balance Sheet reduction - rising to US\$50 billion per month in Q4 - proceeds. The direction of monetary policy is on a collision course with market assumptions of eternally cheap money.

GEOPOLITICAL – CURRENTLY CONTAINED BUT

Trade skirmishes escalate to ‘Trade Wars’, Military Tensions/Action or Regional break-ups (e.g. Italy, Basque or Catalonia in Spain, Brexit), or conflicts (Yemen, South China Sea??) are all imponderables.

The USA has a valid gripe that Euro, Chinese and Canadian trade barriers are each greater against it than are its reciprocal tariffs. Tensions are likely to fester until a new, multi-national agreement on freer-trade is negotiated. [Some parochial but entrenched protectionist measures need to be go]

ASSET PRICE CORRECTION / ANIMAL SPIRITS

Most asset prices – Bonds, Property & Broad Equity Indices - are travelling at very elevated valuations. While ‘Bear Markets’ are seldom predictable, the magnitude of a potential tumble could be severe.

Key Points:

- 1) The aggregate global macroeconomic setting is consistent with financial markets priced for perfection. While no upset is foreseen, consequences are potentially punitive.*
- 2) The ‘consensus’ expectation for only modest inflation pressures ahead is highly questionable;*
- 3) Geopolitical risks may be significant, but are entirely unfathomable, and;*
- 4) The probability is of further gains via financial markets over the coming year to 18 months.*

II) SALIENT ECONOMIC INFLUENCES ON ASSET CLASSES & FINANCIAL MARKETS

ADMINISTERED RATED & BONDS – EASY MONEY IS WANING

The journey back toward 'neutral' interest rates and market-determined Fixed Interest yields, is an upward trend that has begun in flagship USA, in Britain and in Canada. Simultaneously, the unwinding of Quantitative Easing (bond purchases) is proceeding.

US FEDERAL RESERVE SCHEDULED SHRINKING BALANCE SHEET

Monthly caps on System Open Market Account (SOMA) securities reductions		
	Treasury securities	Agency Securities ¹
Oct - Dec 2017	\$6B	\$4B
Jan - Mar 2018	\$12B	\$8B
Apr - Jun 2018	\$18B	\$12B
Jul - Sep 2018	\$24B	\$16B
From Oct 2018 ²	\$30B	\$20B

Source: Wells Capital Mgmt., Market Insights, Nov. 2017

The European Central Bank, having twice reduced its Bond purchases (& may be in 'stealth taper' now), and in June announced its ending QE entirely in 2018.

NZ & Australia are also regarded as likely to commence increasing Administered Rates (OCR's) within our tactical horizon.

INTEREST RATE FORECASTS

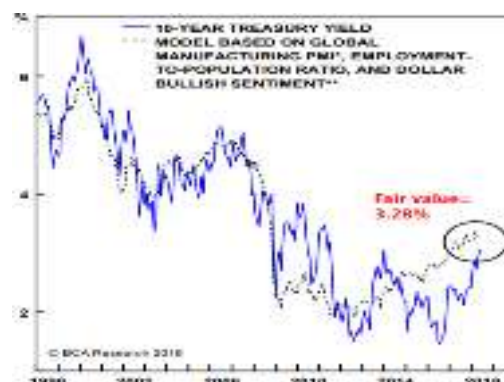
INTEREST RATES	Apr-18	May-18	Today	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19
NZ OCR	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	2.00	2.25
NZ 90-day bill	2.02	2.02	2.00	2.01	2.01	2.00	1.99	2.07	2.32	2.48
NZ 10-yr bond	2.84	2.71	2.98	3.05	3.30	3.40	3.35	3.60	3.65	3.65
US Fed funds	1.75	1.75	1.75	2.00	2.00	2.25	2.25	2.50	2.50	2.50
US 3-mth	2.36	2.30	2.33	2.25	2.50	2.70	2.70	2.95	2.95	2.95
AU Cash Rate	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.75	2.00	2.00
AU 3-mth	2.04	1.98	2.06	1.90	1.80	1.80	1.80	2.05	2.30	2.30

Source: ANZ NZ Market Focus, June 11th 2018

BOND MARKET – QE DISTORTIONS GIVING WAY TO MARKET FORCES

Independent researchers estimate the current state of the US economy justifies a 10-year yield of around 3.28%. The historic model exhibits high correlation, indicating a higher market yield on US 10-year Treasuries should assert.

US 10-YEAR TREASURY YIELDS ARE BELOW AIR VALUE



Source: BCA Research, 'Anticipating the Turn' presentation, May 2018

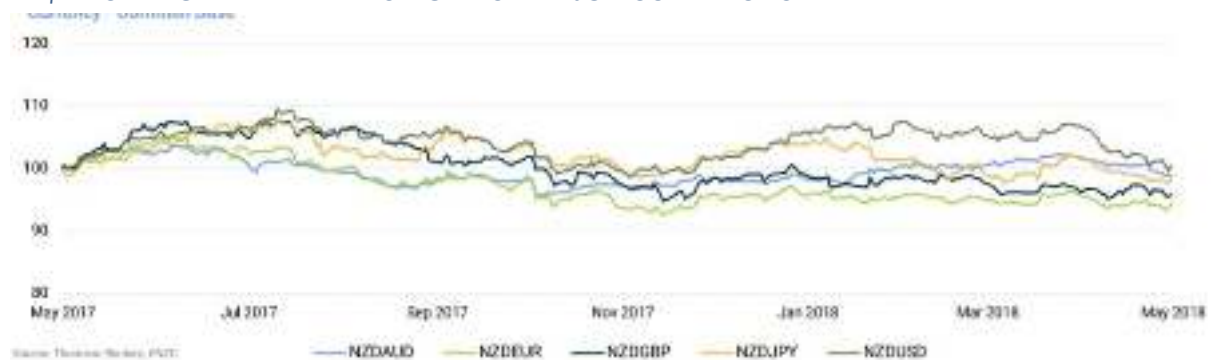
Key Points:

- 1) *A broad global monetary tightening cycle – initially from extremely stimulatory settings toward neutral - is proceeding;*
- 2) *Only the pace of rising rates & yields is regarded as conjectural, and;*
- 3) *While generally accommodative interest rates are expected to linger for most of our tactical horizon, the risk is of further hikes than are broadly expected.*

NZ\$ EXCHANGE RATE

Our NZ\$ reporting currency continues to provide valuable near-term diversity, though has depreciated against most currencies over the past year.

NZ\$ EXCHANGE RATE TRENDS AGAINST MAJOR CURRENCIES



Source: First NZ Capital's, The Daily, June 12th, 2018

ANZ Bank Research provide a synopsis of its exchange rate forecasts.

NZ\$ EXCHANGE RATES AGAINST MAJOR CURRENCIES – PROJECTIONS FOR 2018 & 2019

EX RATES	ACTUAL			FORECAST (END MONTH)						
	Apr-18	May-18	Today	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19
NZD/USD	0.705	0.702	0.70	0.70	0.69	0.67	0.66	0.65	0.65	0.65
NZD/AUD	0.934	0.925	0.93	0.92	0.93	0.93	0.94	0.93	0.93	0.93
NZD/EUR	0.583	0.601	0.60	0.56	0.54	0.52	0.51	0.50	0.50	0.50
NZD/JPY	77.05	76.44	76.93	74.2	71.8	69.0	66.0	64.4	63.1	62.4
NZD/GBP	0.514	0.526	0.52	0.50	0.49	0.47	0.46	0.45	0.45	0.45
NZ\$ TWI	72.5	72.9	73.9	70.8	69.6	67.8	66.5	65.4	65.2	65.1

Source: ANZ Market Focus, June 11th, 2017

Key Points

Our NZ\$'s has depreciated gently against most major currencies over the past year, a trend likely to continue;

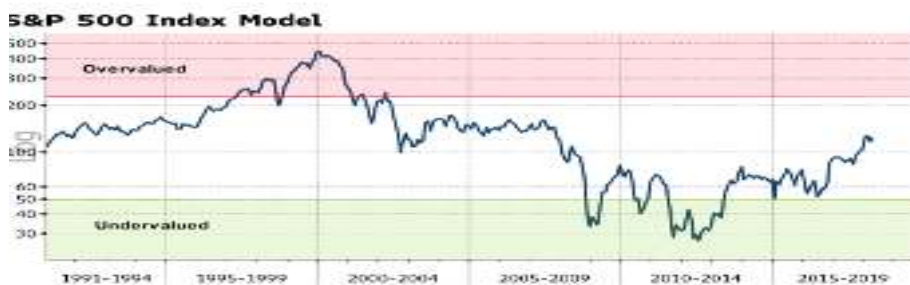
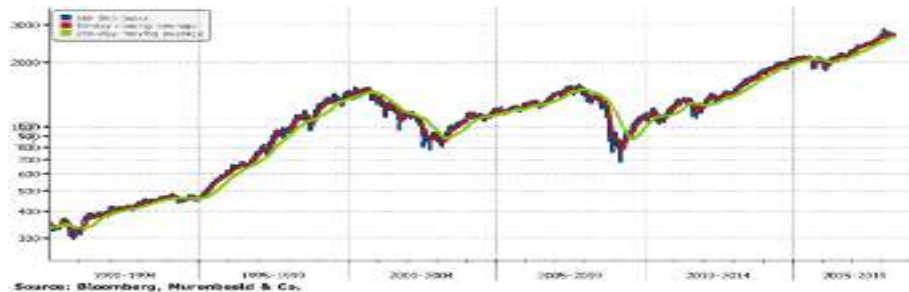
ANZ's projections are that the NZ\$ will not depreciate against the A\$. We are not so sure; and;

A diversity of unhedged currency exposures arising from asset allocation, looks very adequate ahead.

EQUITIES – NOT AS STRETCHED AS SOME COMMENTATORS DECRY

Return of more normal volatility to broad markets in 1Q 2018 unsettled some observers that an upset was imminent. By more dispassionate measure, broad markets are neither over- nor under-valued.

S&P 500 INDEX



Within the above Index, the Consumer Discretionary & Financials sectors are the most fully priced, while the 'IT' and 'Materials' sectors offer relatively better value.

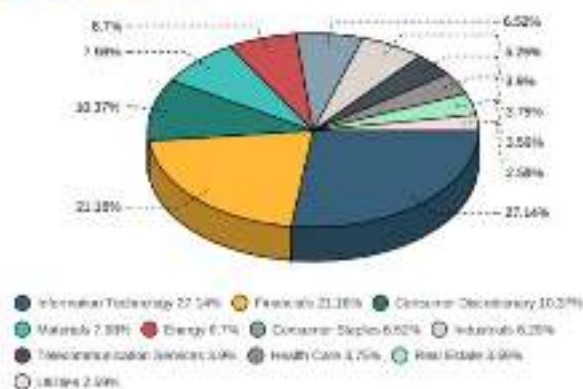
EMERGING MARKETS – BROAD INDEX SECTORS INVERSELY PROSPECTIVE WEIGHTINGS

Emerging Markets thrived on the cheap credit & easy liquidity and facilitated by Quantitative Easing across the Developed World. Both QE and broad EM's have proceeded to unwind as 2018 progressed. Further, previously lucrative Emerging Market regional allocations and holdings may be inversely prospective of economy ahead.

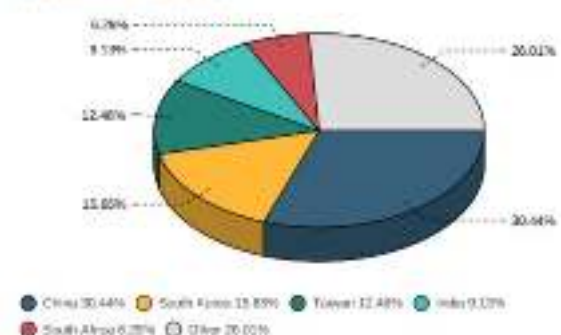
The MSCI Emerging Markets Investible Market Index is inversely prospective. It least exposed to the Materials sectors and is minimally exposed to regions for which accelerating growth is forecast (such as South America).

MSCI EM'S INDEX – DOMINATED BY IT & FINANCIALS IN CHINA & S. KOREA

SECTOR WEIGHTS



COUNTRY WEIGHTS



Source: MSCI March 31st, 2018

Emerging Markets engaged in Resource production, including energy, may enjoy better prospects than Broad Index which served so adequately in recent years.

Key Points:

EM's have benefitted from the abundant global liquidity now unwinding;

The EM universe is of widely disparate economies, regions and sector strengths;

Those Emerging Markets regions and sectors which have been most rewarding in recent years, may be laggards ahead. Active managers should outperform the Index-tracking style.

COMMODITIES – THE FAVOURED TACTICAL ASSET CLASS CURRENTLY

A broad upswing in commodity prices – base-metals, agricultural (aka 'rural'), bulks and energy has been underway since February 2016. It is unlikely fully 'in-the-market' yet.

RBA INDEX OF COMMODITY PRICES – A CONVINCING & BROAD RALLY UNDERWAY



Source: RBA Monetary Policy Statement, May, 2018

Diversified's contention is sustained, strong commodity rally has further to run. Specifically, we find many Institutional investors and their professional advisors, still under-estimating the strength of the metal price cycle underway. PwC in its just released Mining 2018 review concludes, "Although these margins are still too low to incentivize significant new developments, the 25% forecast EBITDA margin for 2018 gets closer ..."

EXCESSIVELY MODEST EXPECTATIONS FOR MINING PROFITABILITY PERSIST

Key ratios	2018 Outlook	2017	2016
Adjusted EBITDA margin	26%	24%	22%
Net profit margin	12%	10%	8%
Return on capital employed	10%	8%	4%
Return on equity	-	11%	5%
Return on capital employed excluding impairment	10%	8%	5%

Source: PwC's 'Mine 2018 Tempting Times', study released May 2018

It is unlikely that bellwether of prosperity, Copper, has seen its' high for this cycle; nor other base-metals. [Note this is not a universal view, with Westpac & Credit Suisse suggesting the highest prices are 'in'.]

Base-metal prices generally peak well ahead of the onset of economic recessions.

RESOURCE PRODUCERS' SHARES – 'MATERIALS' SECTOR AN OPPORTUNITY

Like Australia, Canada's economy & stock market are Resource rich. Despite the run-up since January 2016 [from a very low base], many analysts recognize deep value in the sector at current metal prices.

S&P / TSX MATERIAL SECTOR – STILL CHEAP!



Source: Murenbeeld & Co, 5th May, 2018

OIL PRODUCER'S SHARE PRICES LAG CRUDE GAINS

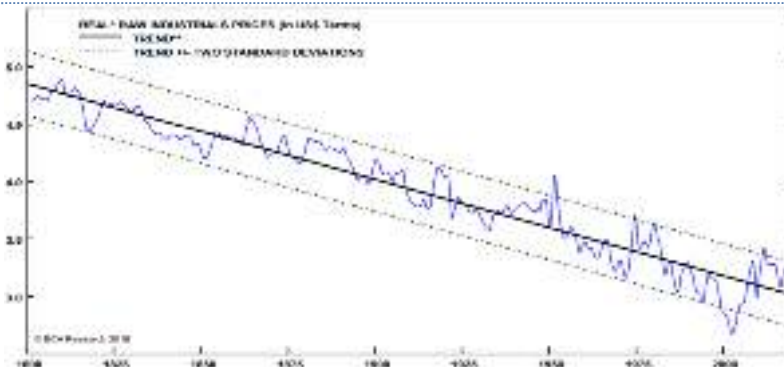
The commodity price of oil has risen by over 60% steadily this past year. Meanwhile, the share price of oil producers (NYSE: XLE as proxy) has risen about 15%.

PHYSICAL OIL VS OIL PRODUCER'S SHARES -BRENT CRUDE (GRN LINE) VS OIL COMPANIES ETF (DARK BLUE LINE)



Source: CNN Money interactive Quotes, 12th June 2018

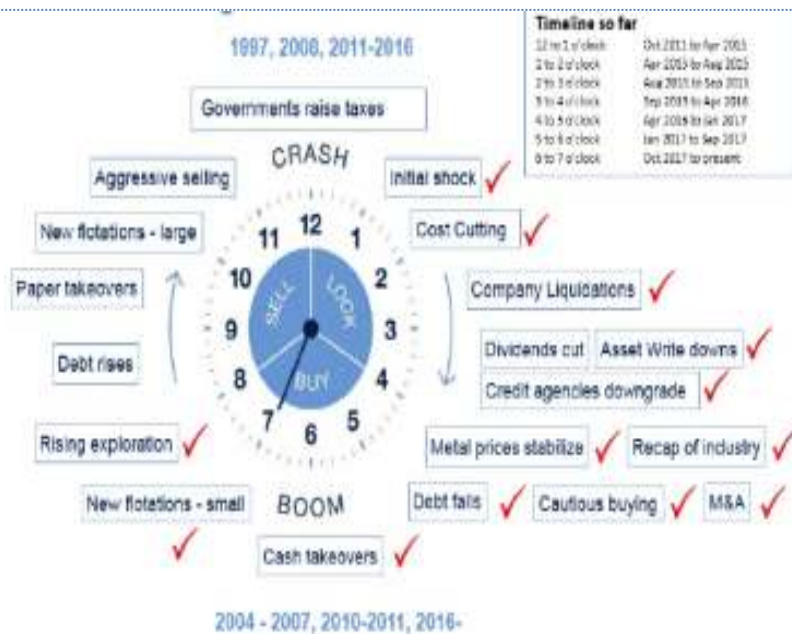
COMMODITIES ARE A TACTICAL, NOT A 'FOREVER', ASSET CLASS



Source: BCA Research, 'Anticipating the Turn' presentation, May 2018

Commodity prices have exhibited a broad, 200-year downtrend, interspersed with periodic rallies. We gauge the current rally in mined commodities has further to run.

INVESTEC MINING CLOCK



Source: Investec Securities estimates, June 14th, 2018

Key Points:

Industrial metal prices have rallied from depressed depths, triggered by rising fundamental demand on relatively neglected & inelastic supply;

Diversified's research finds demand favours higher base-metals prices yet;

Commodity producers offer leverage over physical commodity prices gains, and;

The Commodities asset class is defensive against the corrosive effect of rising inflation on general asset values.

Portfolio Strategy Risks / Vulnerabilities

The following portfolio risks are recognised in Asset Allocations, and could result into portfolios underperforming relative to peers, if unrewarded:

- I. **SHARE MARKET CRASH / 'ANIMAL SPIRITS' FAIL:** Reference Asset Allocations are still significantly exposed to the Equities asset class and are tactically underweight Fixed Interest. (Gross Equities' risk is partially offset by selecting 'Defensive Capable' and 'Long/Short' style for Generalist Equity Managers). Portfolios capital values would unlikely escape a severe market downturn unscathed.
- II. **RESOURCES / MATERIALS ROLL-OVER:** Strategies continue to advocate tactical allocations to selected Resource Producers, as well as to Funds of Commodity Producers'. (The allocation to Emerging & Frontier Market specialty funds is reduced). Portfolios are significantly exposed to the continuation of synchronous global growth including China, fueling sustained strong demand and profitability for producers of Industrial Metals.
- III. **BONDS RALLY:** Asset Allocations are systemically and radically underweight conventional Bonds. Portfolio returns would materially under-perform in the unlikely event the Fixed Interest Asset Class rallied.
- IV. **BOND PROXIES RALLY:** Asset allocations omit asset sectors or classes recognized as Bond Proxies – notably Infrastructure and Property. [Note: Property Class' traditional role as an inflation hedge is served by Industrial Metals].
- V. **NZ\$ APPRECIATES; US\$ DEPRECIATES:** Offshore & notably US\$ assets are not hedged to the NZ\$; our reporting currency. Portfolios will under-perform currency-hedged peers in the event the NZ\$ appreciates materially within our tactical horizon.

III) STRATEGY – ASSET SECTOR RESPONSES

Sector	Comments	Allocation
Cash	'Risk-free' amidst gathering Financial Market risks.	<i>Further increase allocation; Marginally prefer non-NZ\$</i>
<u>Australasian Bonds:</u>	No outstanding value.	<i>Short duration / Favour Resets okay for A\$ Cash repository</i>
<u>Int'l Bonds:</u>	Negative Returns possible	<i>Avoid. Tactically omit conventional Bonds. (Substitute, 'non share market' funds in lieu).</i>
<u>Property</u>	Valuation headwinds as discount rates rise	<i>Zero allocation</i>
<u>Australasian Equities:</u>	Slightly more prospective amidst improved growth outlook. Alpha important to achieving adequate returns.	<i>Exclusively 'Active' & 'Defensive- capable' mgrs.</i>
<u>International Equities:</u>	Still the favoured asset class but growing risks. Broad Emerging Markets face headwinds. Favour L/S styles & dynamic sector rotation.	<i>Reduce overweight by trimming EM allocation. Generalists limited to those with defensive-capability.</i>
<u>Trading/Hedge Funds:</u>	Multi-asset, 'absolute return' style, held as lesser risky amidst expected yield rises.	<i>Employed as substitute for Bonds as diversifier to Equity risks.</i>
<u>Gold Producer's Shares:</u>	Production preferred to Bullion, but less compelling than base-metals.	<i>Reconsider when base-metals roll over.</i>
<u>Commodities / Resources:</u>	Broad Industrial Metals & Energy cycles underway. Good hedge against inflation.	<i>Sell direct Equities at target prices. Add Energy exposure.</i>

SUMMARY OF ASSET ALLOCATION CHANGES RESULTING FROM REVIEW

- A slightly reduction to Growth Assets overweight.
- Tactical positions in Direct Shares of Base-metal producers reduced as TP's achieved.
- Reduce overweight to Int'l Equities' by trimming allocation to Emerging Markets.
- Proceeds of above to non-NZ\$ Cash.
- Consider adding tactical energy investment if opportunistic entry presents.

COMPARATIVE ASSET ALLOCATION - *DIVERSIFIED'S* REFERENCE AA WITH NZ INDUSTRY

Comparison is compiled from the AON Hewitt Investment Update to April 2018, being the average 'Balanced' Asset allocation of AMP, ANZ, Castle Point, Fissure Institutional, Mercer, Milford & Nikko:

	<i>Diversified Balanced</i>	Aon Hewitt 'Average'
Cash		
Aust. & Int'l	12%	12.0%
Fixed Int New Zealand & Australia	8%	12.3%
Fixed Int. Int'l	10%	15.8%
Property		
Australasian & Int'l	0	7.4%
Equity		
New Zealand & Aust	15%	14.7%
International	40%	32.7%
Specialties/ Alternatives/ Trading Funds/ Misc	15%	5.1%

Diversified's reference asset allocation for 'Balanced' investors have several variances from the Institutional average:

- The Reference AA is prospective, whereas the Industry measure is trailing;
- Reference AA is significantly underweight Fixed Interest asset class [18%], compared with the Institutional average [28.1%]. This is consistent with this review's macroeconomic outlook, and assessment of asset class merits.
- The Reference AA omits Bond Proxies including Property;
- Int'l Equities are notionally over-weighted compared with the Institutional average (at 40% to 32.7%). Variance is halved when the Reference's Long / Short funds (approx. 20% of the global generalists selected) is considered.
- Specialties (notably Resource producers' shares) represent a deliberate tactical position.

Adjusting for *Diversified's* tactical asset allocation and the Commodities tilt operating, the reference AA is consistent with a 'Balanced' profile, employing active tactical asset allocation.

REFERENCE ASSET CLASS ALLOCATIONS – JULY, 2018

<i>Risk Profile</i> -----	Balanced	Dynamic
Cash		
Australasian	12.0%	5%
Fixed Interest		
Australasian	8.0%	3%
International*	10.0%*	8%*
Property		
Australasian	-	-
International	-	-
Equity		
Australasian	15.0%	20%
International (global)	20.0%	22%
(specialist)	20.0%	24%
Alternatives/ Specials	15.0%	18%
Income (incl. Prop) : Growth	30 : 70	16 : 84
Australasian : Int'l	35 : 65	28 : 72

- Note: GARS is included under 'Fixed Interest': its sole purpose is to substitute for Bond exposure.

VI) DIVERSIFIED'S INDICATIVE INVESTMENT PORTFOLIOS – JULY 2018

	Balanced	Dynamic
Cash (New Zealand)		
On Call Balance	12%	5%
Fixed Interest (Australasian)		
Enhanced Cash : National Income Securities NABHA	8%	3%
Fixed Interest (Int'l)		
DNP Select Income Fund	5%	4%
Standard Life GARS*	5%	4%
Property		
Equity (Australasian)		
Forté Equity Fund	5%	6%
Salt Long Short Fund	5%	7%
Constellation Australasian Equities Fund	5%	7%
Equity (Int'l)		
RIT Capital Ptnrs Inv. Trust plc	5%	6%
Platinum Int'l Fund	4%	4%
Antipodes Global Fund	3%	4%
VGI Ptnrs (ASX: VG1)	5%	5%
L1 Long Short Fund Ltd	3%	3%
Templeton Emerging Markets IT / or Aberdeen Emerging Opportunities Fund	5%	6%
Genesis Emerging Markets IT	5%	5%
Blackrock Frontier Fund Plc	4%	5%
Schroder Asian Total Return	4%	5%
JP Morgan European Smaller Co's IT	2%	3%
Alternative Investments		
Antofagasta Copper [TP = GBP 11]	0	0
Rio Tinto (TP = US\$60)	3%	3%
NEXA (TP US\$24)	3%	4%
Tribeca Natural Resources Fund	5%	6%
Hecla Mining	3%	3%
NYSE: XLE [opportunistically]	1%	2%
FGS	0	0

Note: Standard Life GARS Fund could as well be included in 'Alternative Investments' category.

**Norman W. Stacey, Investment Analyst,
June 15th, 2018.**