

Crystal ball gazing into 2023

By Greg Smith, Head of Retail at Devon Funds.

With the page having turned on another year, it is time again to engage in the tradition of crystal ball gazing, making big picture predictions on developments and factors that will influence markets and portfolios in the year ahead.

Before that, a quick recap on the year that was. As was the case with the year previous, 2022 was anything but dull. Markets largely moved on from Covid, and as the year wore on, focussed on the fight against another invisible enemy in the form of inflation, one which was fortified further by the war in Ukraine. The concern over the extent and duration of interest rate tightening programs by the world's central banks was a prevalent theme throughout the year.

Looking back on our top 10 predictions from a year ago, there were certainly more hits than misses. The "Great Rotation" from growth to value did indeed click up a few gears, while a harsh dose of reality did set in for investors in crypto-currencies. The kiwi housing market did indeed weaken more than most expected while workers both at home and abroad became more pay-packet conscious. The groundswell for a third supermarket operator in NZ was not as loud as it could have been, but the prediction that tensions would ratchet higher on the geopolitical front proved to be somewhat of an understatement, given Russia's invasion in the Ukraine.

Markets generally were not resilient, although the kiwi market did hold up better than many counterparts....[READ MORE](#)

MARKET INDICES

Index	Region	Monthly Return	1 Yr. Return
S&P/NZX50G	NZ	-0.7%	-12.0%
S&P/ASX200G	AUSTRALIA	-3.2%	-1.1%
MSCI World Index	GLOBAL	-4.2%	-17.7%
S&P500	USA	-5.8%	-18.1%
FTSE100	UK	-1.5%	4.7%
NIKKEI 225	JP	-6.5%	-7.3%
NZ 90 Day Bank Bill	NZ	0.4%	2.2%
Bloomberg Global Aggregate Index (NZD)	GLOBAL	-1.2%	-11.7%

AT A GLANCE

Prices as at 30 DECEMBER 2022

DEVON ALPHA FUND	\$2.0773
DEVON AUSTRALIAN FUND	\$1.5364
DEVON DIVERSIFIED INCOME FUND	\$1.4387
DEVON DIVIDEND YIELD FUND	\$1.8868
DEVON GLOBAL IMPACT BOND FUND	\$1.3749
DEVON GLOBAL SUSTAINABILITY FUND	\$1.4485
DEVON TRANS-TASMAN FUND	\$4.4162
DEVON SUSTAINABILITY FUND	\$3.1271

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DEVON ALPHA FUND

FUND OUTLINE

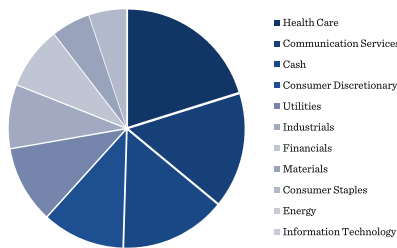
The **Alpha Fund** invests in a concentrated portfolio of approximately 10 to 15 select companies predominantly listed on the NZ and Australian share markets.

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.

KEY HOLDINGS



ASSET ALLOCATION



ALLOCATION

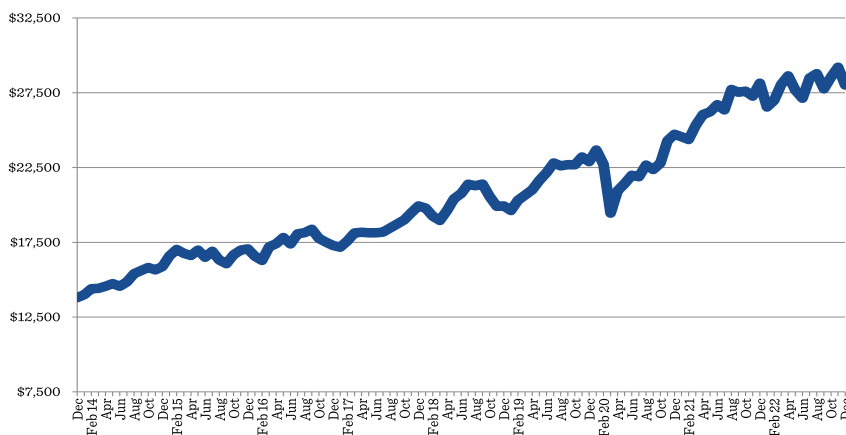
New Zealand Equities	26.0%	Cash	8.8%
Australian Equities	65.2%	Total	100.0%
Currency Hedge	0.2%		

	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a	Since Inception
Devon Alpha Fund	-4.1%	0.9%	-0.4%	7.0%	7.1%	8.9%
OCR + 5%	0.7%	2.1%	3.9%	1.5%	1.5%	2.1%

Devon Alpha Fund returns are after all fees and expenses, but before tax which varies by investor.
*The benchmark for Alpha changed to OCR + 5% from 1 September 2022

NET PERFORMANCE

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



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](#)

COMMENTARY

The Alpha strategy was weaker in December, in what proved to be one of the more challenging months that the fund has endured over the past three years. The reason for the decline in its value in December was that we had positioned the portfolio in a way which reflected our view that the valuations across a number of high-quality cyclical stocks were beginning to look compelling. This portfolio structure was not rewarded during the month, but we are confident that as we progress through 2023 that we will enjoy strong positive returns from many of these investments. This includes companies such as James Hardie, which despite facing ongoing operational headwinds due to the challenging US construction market, is extremely well positioned to enjoy investor support as the volatility in the mortgage market stabilises and building activity levels begin a process of recovery. Our view also remains that the opportunity set in Australia will be more productive than that in New Zealand over the next 12-months.

PORTFOLIO MANAGER

Slade Robertson



Slade has primary responsibility for stock selection and portfolio construction for the Alpha, Australian and Diversified Income funds. Slade is also the Managing Director at Devon and has overall responsibility for the business. Slade has over 20 years' industry experience.



DEVON AUSTRALIAN FUND

FUND OUTLINE

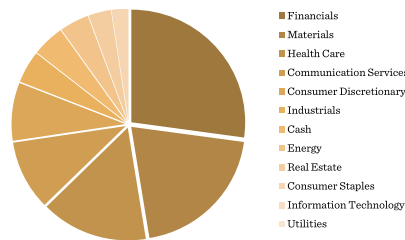
The Australian Fund invests in a select portfolio of companies, which are primarily Australian listed companies.

The Australian market is much larger than the New Zealand market and offers exposure to a number of sectors that are not available in New Zealand. The Australian dollar currency exposure of this Fund is typically unhedged.

KEY HOLDINGS



ASSET ALLOCATION



ALLOCATION

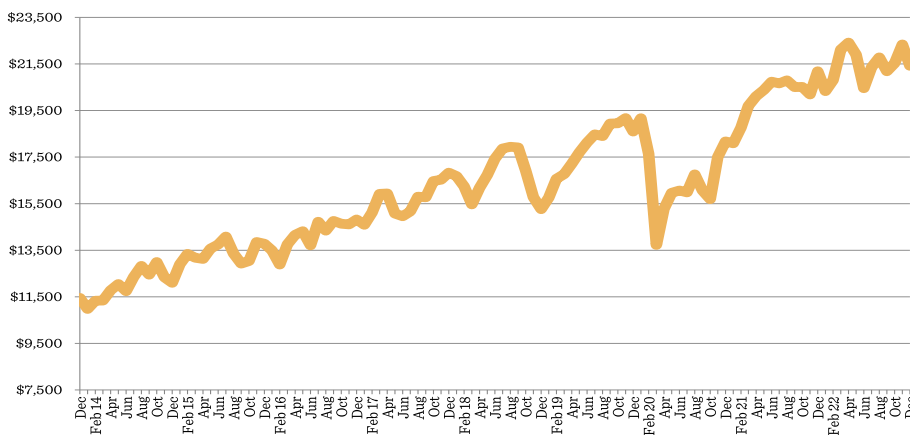
Table with 2 columns: Allocation Category and Percentage. Rows include New Zealand Equities (0.0%), Australian Equities (93.8%), Cash (6.2%), and Total (100.0%).

Table with 7 columns: Performance Metric, 1 Mth, 3 Mth, 1 Yr, 3 Yr p.a, 5 Yr p.a, and Since Inception. Rows include Devon Australian Fund and ASX200 Index Gross (NZD).

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



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

COMMENTARY

The Australian strategy performed broadly in-line with its benchmark during the month, although it was a challenging month for the ASX. The stocks which enjoyed the most support included those in the Mining and Resources sectors. Within this portfolio, we had exposure to Rio Tinto and BHP which outperformed, returning 6.2% and 0.2% respectively. This reflected a growing level of optimism that the Chinese government will undertake a more growth-oriented approach to policy, which should provide a positive influence on demand for Australian iron ore and minerals. Another positive contributor was QBE, whose share price jumped by 4.4%. Investors recognised the opportunity for this business, and the broader general insurance sector, to lift premiums and to leverage off rising interest rates. Although the Australian market struggled in December, we remain of the view that this economy and many of its stocks are well positioned to generate strong positive returns in 2023.

PORTFOLIO MANAGER

Slade Robertson



Slade has primary responsibility for stock selection and portfolio construction for the Alpha, Australian and Diversified Income funds. Slade

is also the Managing Director at Devon and has overall responsibility for the business. Slade has over 20 years' industry experience.



DEVON DIVERSIFIED INCOME FUND

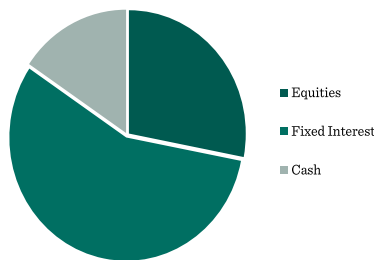
FUND OUTLINE

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.

KEY HOLDINGS



ASSET ALLOCATION



ALLOCATION

New Zealand Equities	17.3%	Bonds	55.8%
Australian Equities	9.2%	Cash	17.7%

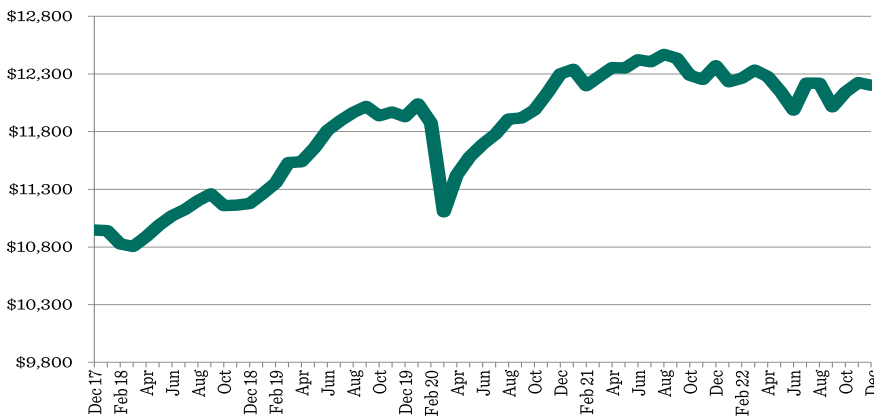
PERFORMANCE

	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a	Since Inception
Devon Diversified Income Fund	-0.2%	1.6%	-1.4%	0.7%	2.2%	3.0%
OCR + 1.5%	0.4%	1.3%	3.8%	2.5%	2.7%	2.9%

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



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](#)

COMMENTARY

Global bond yields rallied during December, with the interest rate on the US 10-year Treasury closing the month at 3.83%. Investors closely watched the positioning of the US Federal Reserve at their December meeting after US core CPI came in below expectations in November (rising by only 0.2%). Despite this improving data, Chairman Jerome Powell raised its benchmark rate by 0.5%. Although this was their smallest hike in 7-months, the forecasts included within their Summary of Economic Projections indicated there will be an additional 0.75% of hikes by the end of 2023. Interestingly in Australia, the RBA lifted rates by 0.25% (their eighth consecutive move) but in the associated minutes of the meeting, it was apparent that the RBA did actually consider not raising the cash rate at all at their latest meeting. The RBNZ did not have a policy meeting in December.

PORTFOLIO MANAGER

Slade Robertson



Slade has primary responsibility for stock selection and portfolio construction for the Alpha, Australian and Diversified Income funds. Slade is also the Managing Director at Devon and has overall responsibility for the business. Slade has over 20 years' industry experience.

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DEVON DIVIDEND YIELD FUND

FUND OUTLINE

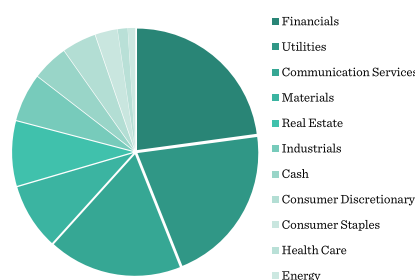
The **Devon Dividend Yield Fund** invests in a carefully selected portfolio of New Zealand and Australian listed companies.

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.

KEY HOLDINGS



ASSET ALLOCATION



ALLOCATION

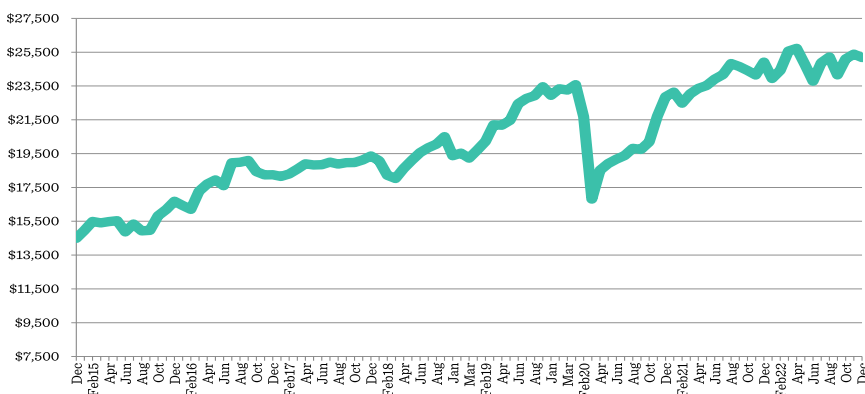
New Zealand Equities	62.3%	Cash	4.4%
Australian Equities	33.2%	Total	100.0%
Currency Hedge	99.8%	Yield	6.3%

PERFORMANCE	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a	Since Inception
Devon Dividend Yield Fund	-0.8%	4.3%	1.1%	2.7%	5.4%	9.8%
50:50 NZX50 & ASX200 Index Gross	-1.9%	6.5%	-6.5%	2.7%	6.8%	10.5%

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 1 January 2011



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](#)

COMMENTARY

The reopening of the Chinese economy post-Covid remained the dominant investment theme during the month, with local equity markets once again led by commodity stocks. Our investments in BHP and RIO significantly outperformed the ASX, up 0.2% and 6.2% respectively. We have used these strong stock performances to take profits and reduce our exposure to the sector.

Our investments in the high yielding and well capitalized banking sector disappointed, as bond rate volatility and the possibility of tighter economic conditions made some investors nervous about the longevity of improving banking profitability.

Our exposure to the NZ electricity generation sector performed well, with all our investments exceeding the NZX50 index. Meridian (+7%) and Contact (+2.9%) were our best performers. Contact Energy's sustainability credentials were globally acknowledged by its inclusion in the Dow Jones Asia Pacific Sustainability Index. This index is the longest running and most prestigious global benchmark for corporate sustainability.

PORTFOLIO MANAGER

Mark Brown



Mark has primary responsibility for stock selection and portfolio construction for the Dividend Yield Fund and the New Zealand Equity fund. Mark is also responsible for overseeing the overall research and investment process at Devon.

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DEVON TRANS-TASMAN FUND

FUND OUTLINE

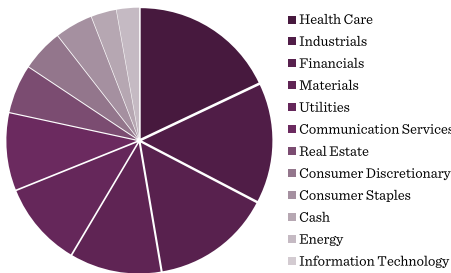
The **Trans-Tasman Fund** provides a broad and actively managed exposure to the New Zealand and Australian equity markets.

This Fund invests in a select portfolio of well researched companies, which are primarily New Zealand and Australian listed companies. The Australian dollar currency exposure is typically unhedged.

KEY HOLDINGS



ASSET ALLOCATION



ALLOCATION

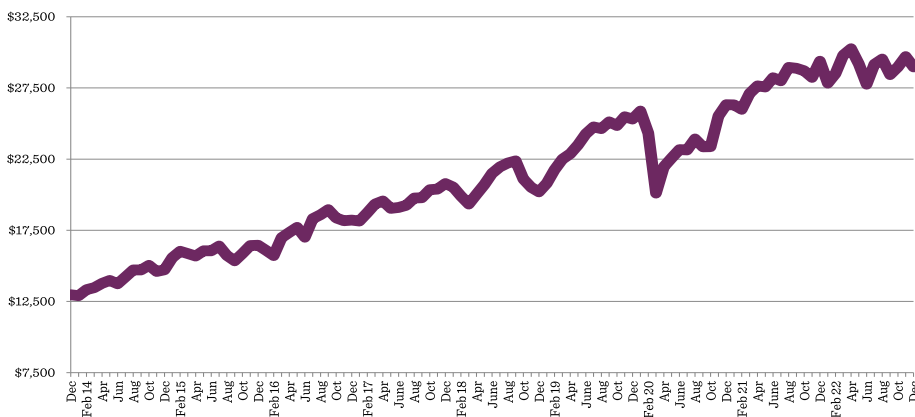
New Zealand Equities	43.6%	Cash	2.6%
Australian Equities	53.8%	Total	100.0%

PERFORMANCE	1 Mth	3 Mth	1 Yr	3 Yr p.a	5 Yr p.a	Incep- tion
Devon Trans-Tasman Fund	-2.4%	1.9%	-1.5%	4.6%	6.8%	8.3%
50:50 NZX50 Gross & ASX200 Index Unhedged	-2.2%	3.4%	-6.0%	3.3%	6.5%	9.0%

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



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](#)

COMMENTARY

The Trans-Tasman strategy performed broadly in line with its underlying benchmark during the month. This capped off a very strong year of relative performance for the portfolio in a challenging market environment. Key contributors over the month included overweights in Rio Tinto, QBE and Contact Energy and an underweight position in Ryman, while key detractors included Sky City, Goodman Group and ResMed.

Telstra traded flat over the month, but we continue to expect strong out-performance ahead over 2023. On the earnings front, we see potential for earnings to be towards the top end of guidance due to a recent competitor data breach (Optus), a weaker A\$ benefiting Digicel earnings and potentially an improved roaming result given the strong recovery in travel. The larger medium-term catalyst is the potential sell-down of their infrastructure assets. The long-term contracts, predictable cashflows and growth projects liken their InfraCo assets to recent telecommunication asset transactions, which achieved high multiples.

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. Tama holds co-responsibility for Devon's Trans-Tasman Funds. Tama is widely regarded as a leading expert on resource and mining stocks.



DEVON SUSTAINABILITY FUND

FUND OUTLINE

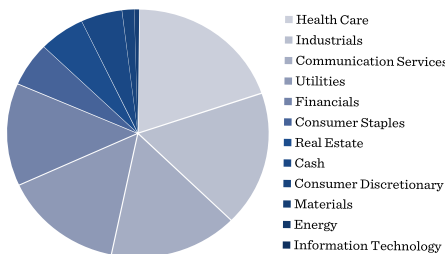
The **Devon Sustainability Fund** invests in a select portfolio of well researched New Zealand and Australian listed companies.

The Fund looks to invest in companies that score highly on overall environmental, social and corporate governance performance. The Fund also employs an ethical screen which will prohibit investment into certain companies and sectors.

KEY HOLDINGS



ASSET ALLOCATION



ALLOCATION

New Zealand Equities	50.3%	Cash	3.0%
Australian Equities	46.6%	Total	100.0%

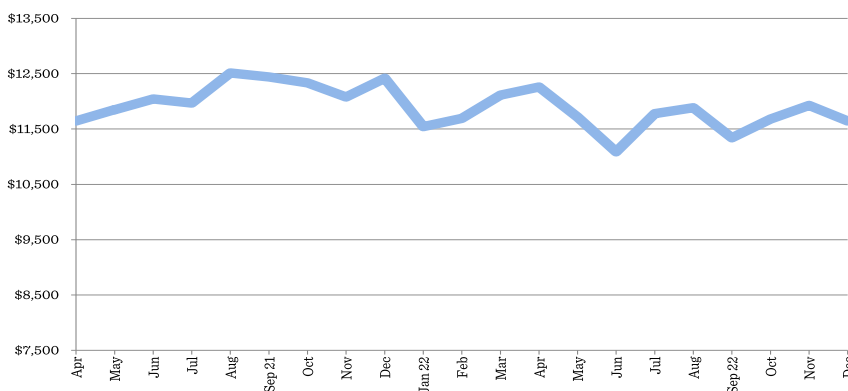
PERFORMANCE

	1 Mth	3 Mth	1 Yr p.a	2 Yr p.a	Since Inception
Devon Sustainability Fund	-2.3%	2.7%	-6.3%	1.8%	6.7%
50:50 NZX50 Portfolio Index & ASX200 Index	-2.1%	5.4%	-6.6%	1.0%	6.5%

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

NET PERFORMANCE

Based on \$10,000 invested at 31 August 2020



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

COMMENTARY

Top positive contributors during December were EBOS (+7.2%), A2 Milk (+11.0%) and Meridian (+7.1%). The detractors to performance included Ryman (-18.4%), Nine Entertainment (-12.4%) and Goodman Group (-8.4%).

Healthcare company EBOS outperformed as investors sought out quality, defensive names as we head into 2023. The healthcare company has continued to prove its resilience in the current environment due to its diversified business. Its Healthcare division represents 80% of company earnings whilst Animal Care is responsible for 20%. Woolworths announced during the month that it had acquired competitor pet care company Petspiration. This demonstrates the importance of EBOS's Animal Care division which is expected to grow by high-single digits over the medium-term. EBOS's Animal Care business is well positioned to take advantage of the boom in pet ownership as well as increased spend on pets which has accelerated during COVID. Despite having performed well, EBOS's valuation still remains attractive, with its defensive earnings profile.

PORTFOLIO MANAGER

Victoria Harris



Victoria has primary responsibility for stock selection and portfolio construction for the Australian and Sustainability funds.

Victoria has over 10 years' experience in the industry across a broad range of markets, including ESG.

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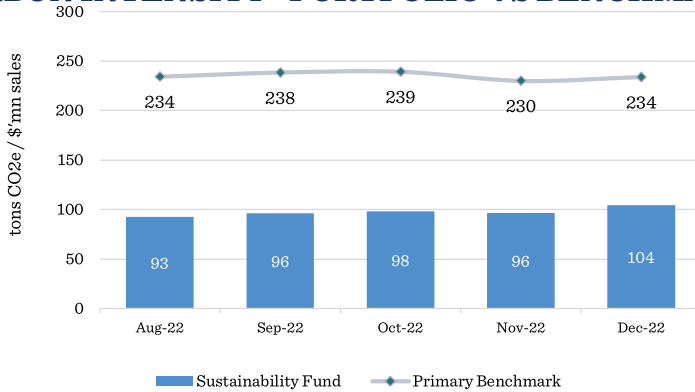
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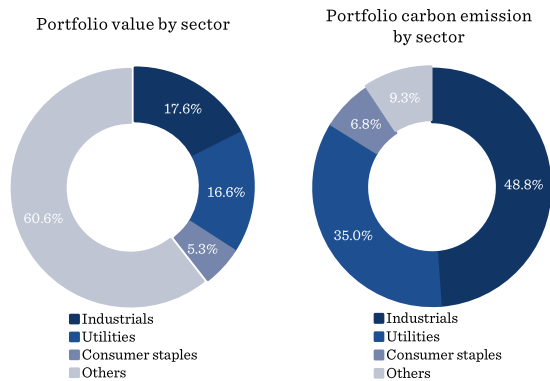


DEVON SUSTAINABILITY FUND

CARBON INTENSITY - PORTFOLIO VS BENCHMARK



PORTFOLIO CARBON EMISSIONS BY KEY SECTORS



The industrials, utilities and consumer staples sectors make up 94.3% of the portfolio by value, but they account for 42.6% of the carbon emissions in the portfolio.

The materials, utilities, and health care sectors make up 36.2% of the portfolio by value, but they account for 84.4% of the carbon emissions in the portfolio.

ESG PORTFOLIO SUMMARY

	MSCI ESG Ratings	MSCI ESG Quality score	
Portfolio	AA	7.36	Portfolio Sustainability Fund
Benchmark	A	6.78	Primary Benchmark 50:50 composite S&P/NZX50 Portfolio Index & S&P/ASX200G Index

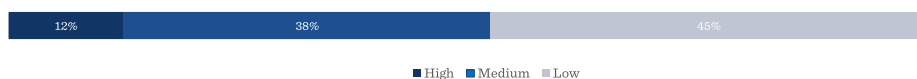
PERFORMANCE	1 Mth	3 Mth	6 Mth	1 Yr	Since Inception
ESG relative performance	8.6%	13.7%	14.4%	12.2%	6.5%

*ESG Relative Performance is the MSCI ESG Score of the Devon Sustainability fund compared to the MSCI ESG Score of the Benchmark

PORTFOLIO HOLDING'S DISCLOSURE SUMMARY

% of holding companies doing ESG reporting	95.2%
% of companies reporting to TCFD standards	69.0%
% of companies with a modern slavery statement	69.0%
% of companies with carbon emission reduction targets	73.8%

CLIMATE CHANGE RISK BY PORTFOLIO HOLDINGS



STEWARDSHIP

As we wrap up 2022, we thought we would touch on some key stewardship and ESG themes. Firstly, at Devon last year we engaged with many companies around emissions reduction targets. This was the dominant focus for corporates as the 2030 gatepost for necessary reductions fast approaches. Companies such as Cleanaway and CSL made significant progress by setting more specific targets around sustainability. Secondly, the Great Resignation in 2022 has led to a number of CEO/CFO changes and board turnover which accelerated in the second half of 2022. This cast a particular focus on governance and executive diversity. Appropriate incentive structuring was another outcome here with many companies moving towards incorporating non-financial KPIs in short-term plans. Finally we also saw a number of major cyber security and data breaches occur during the year, a trend which unfortunately is gathering momentum.

PORTFOLIO MANAGER

Victoria Harris



Victoria has primary responsibility for stock selection and portfolio construction for the Australian and Sustainability funds. Victoria has over 10

years' experience in the industry across a broad range of markets, including ESG.



DEVON GLOBAL IMPACT BOND FUND

DURATION

Sector	Contribution to Duration (Years)		
	Account	Benchmark	Difference
Cash & Cash Equivalents	-0.00	-	-0.00
US Government	0.75	1.04	-0.29
Credit*	4.56	4.90	-0.34
Asset Backed Securities	0.01	0.01	0.00
Mortgage Backed	1.24	0.79	0.45
Commercial Mortgage	0.10	0.04	0.07
Other	0.01	0.10	-0.09
Cash Offset	-	-	-
	6.67	6.87	-0.20

The Fund invests into the Wellington Global Impact Bond Fund, managed by Wellington Management. Wellington Management is one of the world's leading investment management firms with over US\$1 trillion in assets under management worldwide across a broad range of asset classes. They have been providing innovative investment solutions to clients for more than 85 years. Wellington Management seeks to understand the world's social and environmental problems and to identify and invest primarily in debt issued by companies and organisations that they believe are addressing these needs in a differentiated way through their core products, services and projects. The Wellington Global Impact Bond Fund aims to improve access to, and the quality of, basic life essentials, reduce inequality and mitigate the effects of climate change.

CREDIT RATING

Quality	Percent of Market Value		
	Account	Benchmark	Difference
Cash	10.53	0.26	10.28
AAA	47.21	40.65	6.56
AA	12.33	11.80	0.54
A	10.11	32.41	-22.30
BBB	13.06	14.56	-1.50
BB	4.89	0.01	4.88
B	2.05	-	2.05
Below B	0.17	-	0.17
Cash Offset	-1.02	-	-1.02
Not Rated	0.67	0.31	0.35
	100.00	100.00	

They seek to identify securities which it believes fall into three primary impact categories: life essentials, human empowerment and the environment. Within these categories the Fund will invest across "Impact Themes" including, but not limited to the following:

Life Essentials: affordable housing, clean water and sanitation, health, sustainable agriculture and nutrition.

Human Empowerment: digital divide, education and job training, financial inclusion, safety and security.

Environment: alternative energy, resource efficiency and resource stewardship.

*Duration & Credit Rating as at 30 December 2022

DEVON GLOBAL SUSTAINABILITY FUND

The Fund invests into the Wellington Global Stewards Fund, managed by Wellington Management. Wellington Management is one of the world's leading investment management firms with over US\$1 trillion in assets under management worldwide across a broad range of asset classes. They have been providing innovative investment solutions to clients for more than 85 years. Wellington Management seeks to invest in companies globally, that generate high return on capital relative to their peers, and whose management teams and boards display exemplary stewardship to sustain those returns over time. Wellington define stewardship as how companies balance the interests of all stakeholders (customers, employees, communities and the supply chain) in the pursuit of profits and how they incorporate material environmental, social and governance (ESG) risks and opportunities in their corporate strategy. The underlying Wellington Fund differentiates itself by:

Long-term horizon – the intention is to hold stocks for over 10 years. The belief is the longer the holding period, the greater the potential performance benefits from superior stewardship.

Highly selective – typically 35-45 stocks, only relying on their own internal ESG research.

Active engagement – holding those in charge of investee companies to account and encouraging companies to commit to net zero carbon emissions by 2050 in alignment with the Paris Agreement.

PERFORMANCE	1 Mth	3 Mth	6 Mth
Devon Global Impact Bond Fund	-1.0%	1.1%	-2.3%
Bloomberg Global Aggregate Index Hedged NZD	-1.2%	0.8%	-2.9%

PERFORMANCE	1 Mth	3 Mth	6 Mth
Devon Global Sustainability Fund	-2.6%	7.1%	3.7%
MSCI All Country World Index in NZD, 50% hedged to NZD	-5.2%	2.6%	0.8%

*Benchmark performance figure is indicative only and will be finalised in the mid month report

Please note that monthly reports will be produced for the Devon Global Impact Bond Fund and Devon Global Sustainability Fund later this month. These reports will include data on top holdings, performance, asset allocation, and fund commentaries. These reports will be sent out separately from those for Devon's other retail funds each month and will be available on the Devon Funds website.

KEY HOLDINGS*



*Key Holdings as at 30 December 2022

Devon Funds Management Limited

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