

# Yarra Australian Equities Fund

## Gross returns as at 30 April 2021

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception* % p.a.
Yarra Australian Equities Fund	2.66	9.71	35.39	6.81	8.92	8.21	10.70
S&P/ASX 200 Accumulation Index <sup>†</sup>	3.47	7.54	30.76	9.49	10.27	8.35	9.41
Excess return (before fees) <sup>‡</sup>	-0.81	2.17	4.63	-2.68	-1.35	-0.13	1.29

Past performance is not a reliable indicator of future performance. Taxes payable by investors have not been taken into account. The figures shown have been provided for illustrative purposes – they are unaudited and subject to change. The total returns shown are gross of all fees, meaning they do not reflect the deduction of any investment management fees which would reduce returns and assume reinvestment of all distributions. Investment in the fund is not available on a fee free basis and this should be factored into any analysis of past performance.

## Net returns as at 30 April 2021

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception* % p.a.
Yarra Australian Equities Fund	2.58	9.47	34.19	5.83	7.91	7.20	9.70
S&P/ASX 200 Accumulation Index <sup>†</sup>	3.47	7.54	30.76	9.49	10.27	8.35	9.41
Excess return (after fees) <sup>‡</sup>	-0.89	1.93	3.43	-3.66	-2.36	-1.14	0.29

Past performance is not a reliable indicator of future performance. Taxes payable by investors have not been taken into account. The figures shown have been provided for illustrative purposes – they are unaudited and subject to change. The total returns shown are prepared on an exit to exit basis – they include all ongoing fees and expenses and assume reinvestment of all distributions.

\* Inception date Yarra Australian Equities Fund: July 1996

<sup>†</sup> The benchmark for the Yarra Australian Equities Fund has been amended since the Fund's inception. Effective 28 February 2008 the benchmark is the S&P/ASX 200 Accumulation Index, replacing the S&P/ASX 200 ex Property Accumulation Index Monthly. Further information on changes to the Fund's benchmark is available upon request.

<sup>‡</sup> Excess return: The difference between the portfolio's return and the benchmark return.

### Market review

Australian equities continued to generate strong returns in April, rising above pre-pandemic levels for the first time.

The S&P/ASX 200 Accumulation Index returned +3.8% for the month, taking its 12-month return to +30.7%. The index lagged global indices, with the MSCI World Index climbing +4.1% and the S&P500 returning +5.3%.

Gold (+9.6%) and Information Technology (+9.7%) were among the top performing sectors as the 'reflation trade' partially reversed, with the Australian 10-year bond yield falling 10 bps to 1.69%. Within the former, Newcrest Mining (NCM, +8.6%), Northern Star (NST, +10.9%) and Evolution Mining (EVN, +13.5%) partially recovered declines from prior periods. Within tech, Afterpay (APT, +15.9%) announced +100% sales growth in 3Q21, largely driven by strong momentum in its US business.

Other strong performers were online services companies Domain Holdings (DHG, +21.0%), REA Group (REA, +11.7%) and Carsales.com (CAR, +11.7%), and waste management company Cleanaway Waste Management (CWY, +29.5%) after it announced the acquisition of Suez's recycling and recovery business in Australia for \$2.5bn.

Conversely, Energy (-4.9%) and Consumer Staples (-2.5%) weighed on the benchmark. In the former, Origin Energy (ORG, -11.3%) announced an 8% downgrade to earnings guidance in its Energy Markets business. In the latter, China-exposed companies A2 Milk (A2M, -7.8%), Treasury Wine Estates (TWE, -3.0%) and Blackmores (BKL, -10.2%) were among the worst performers.

### Portfolio review

#### Key Contributors

**Woolworths (WOW, underweight)** – the supermarket company underperformed after announcing its 3Q21 sales figures during the period. In Australian Food (61% of group EBIT), sales declined 2.1% y/y as the division cycled strong sales during the onset of COVID-19. However, this was partially offset by a strong performance in its online division, recording 91% growth and 8% penetration (versus 4% in the pcp). Our underweight position reflects concerns at the stock's stretched valuation at 24.2 times forward earnings, which in our view doesn't yet reflect conditions normalising post-COVID. Furthermore, the outlook for discount department store Big W remains challenged, particularly considering the threat of online and the need to rationalise excess store capacity.

**Aristocrat Leisure (ALL, overweight)** – the gaming company continued to outperform following management's roundtable late in the prior month. Commentary suggested Land Based Gaming (45% of group EBIT) was tracking ahead of expectations, with 92% of venues now open, and Digital (55% of group EBIT) was benefiting from a permanent – rather than temporary – step-up in activity following COVID. Our investment thesis is premised on ALL's strong growth profile following the resolution of the COVID-19 crisis. ALL has a dominant position in Land Based Games and is set to benefit from significant opportunities from Digital, which offers a wide range of outcomes. Lastly, the stock appears undervalued at 27.5 times forward earnings when considering the Industrials Ex-Financials Index trades at 28.2 times and ALL's superior long-term growth potential.

**Carsales.com (CAR, overweight)** – the online automotive classifieds company outperformed during the period without any material news. Our positive view remains premised on the belief CAR should benefit from attractive earnings growth, conservative accounting (with low capitalisation of research and development investment) and undervalued international businesses. Further, we see CAR's valuation as attractive relative to peers, trading at 31.1 times forward earnings versus REA Group (REA) at 52.0 times.

#### **Key Detractors**

**Origin Energy (ORG, overweight)** – the company underperformed after downgrading EBITDA guidance by 8% in its Energy Markets business during the period. Management lowered its range from \$940-1,020mn (from \$1,000-1,040mn) due to an adverse ruling on a gas dispute with Beach Energy (BPT) and ongoing electricity market weakness. However, at a group level APLNG partially offset this weakness, with ORG announcing it expects a FY21 cash distribution of more than \$650mn from the plant amid higher-than-expected production and gas prices. We remain overweight the stock. Following its initiatives, ORG is now in a stronger position to withstand lower electricity wholesale prices, which we view as being at unsustainably low levels. The company has >\$4bn of liquidity – which can cover all debt maturities in the next 36 months – while APLNG has a lower distribution breakeven of US\$27-31 per barrel and \$1.2bn in cash (as at 30 June 2020).

**TPG Telecom (TPG, overweight)** – the telco underperformed as the surprise resignation of the Chair, announced late in the previous month, continued to weigh on the stock. Despite the lack of clarity around the circumstances of his resignation, we remain overweight the stock. Our positive view remains premised on the recently completed Vodafone merger, which in our view will unlock significant synergies. The combined entity is well placed to harness its infrastructure, scale and balance sheet to disrupt incumbents Telstra (TLS) and Optus through its lower-cost structure, as well as via new products such as Fixed Wireless.

**JB Hi-Fi (JBH, overweight)** – the electronics retailer underperformed after announcing a 3Q21 trading update and a CEO transition plan. Trading was largely in line with expectations, with JBH Australia recording +11.5% y/y growth and The Good Guys up +5.8% y/y. However, the transition –

whereby The Good Guys managing director takes the helm in August – was a surprise and may have increased market uncertainty during what is an increasingly unpredictable sales environment. We remain overweight the stock. We believe JBH is under capable hands under the new CEO, who previously ran the business from 2010 to 2014. We continue to believe the market underestimates JBH's ability to grow across different trading conditions, which is not reflected in its valuation at 14.5 times 12-month forward earnings. In regards to The Good Guys, execution has improved significantly and management is now focused on maintaining the strong increase in customers as homewares benefit from the COVID-19 pandemic, which could add significant upside.

#### **Key Purchases**

**Latitude Group (LFS)** – we took part in the IPO during the period, with our positive view of the consumer finance business based on several factors. Firstly, we saw its valuation as attractive at 9.7 times our estimate of FY22 earnings, which we believe more than compensates for its small adjusted free float (28%) and selling overhang, and attractive versus peers which trade on an average multiple of 11 times. Secondly, we see LFS as positively leveraged to the strengthening Australian consumer, both through sales and credit expenses. Lastly, we see LFS as a beneficiary of COVID-affected categories including travel services, which we do not believe is captured in market expectations.

**IGO Limited (IGO)** – we increased our position in the lithium-nickel miner during the period. Our thesis is premised on the miner's recent \$US1.4bn Greenbushes acquisition and its existing portfolio of high-quality assets. We support the acquisition for several reasons. Not only does it give IGO exposure to a high-quality, long-dated asset (>20 years mine life), but it also completes IGO's suite of battery commodities with the company already producing nickel, copper and cobalt. We also think the purchase price was reasonable, with Greenbushes likely to be NPV and EPS accretive earlier than FY23. We also hold a positive view of IGO's Nova asset – a world-class reserve which supports an increasing production profile – and expect its Tropicana gold asset to be divested in the short term, further supporting the balance sheet.

#### **Key Sales**

**Vocus Group (VOC)** – we reduced our position as the telco traded within range of the \$5.50 per share takeover offer from the Aware Super / MIRA consortium. We remain overweight, as we view the offer as credible, and are more optimistic it will result in a binding offer following management's recent improvements. The management team has made significant progress in integrating and simplifying the various acquired businesses, unifying its product offering and increasing customer product penetration – driving significant longer-term revenue and margin opportunities.

**Healius (HLS)** – we reduced our position following recent outperformance but remain overweight the company. We hold a positive view of its pathology and diagnostic imaging divisions and continue to regard its valuation as supportive. The sale of the medical centre business last year enables

management to focus on and invest in the pathology, day surgery and diagnostic imaging businesses, which are return on invested capital (ROIC) accretive and have significant margin opportunities. We do not believe this is captured by consensus, with HLS trading at 21.8 times forward earnings – well below the Industrials ex-Financials Index at 28.2 times.

**Tyro Payments (TYR)** – we trimmed our position following recent outperformance but remain overweight the payment solutions provider. As the lead provider of software that allows payment terminals to be integrated into point-of-sale (POS) systems, TYR remains in a defensible position versus peers, including the banks which rely on a less sophisticated intermediary. Moreover, short-term headwinds are more than reflected in TYR's valuation, with the stock trading at 6.4 times forward sales – a significant discount to its technology peers.

### Key Active Overweights

**ANZ Bank (ANZ)** – we are overweight ANZ on the grounds that the bank is positioned strongly for an earnings and dividend recovery post-COVID, with capital management initiatives likely as bad debts turn out to be more benign than feared. While there are challenges to its outlook – including persistent top-line pressures from lower interest rates – the bank is able to offset these pressures by cutting costs at a superior rate to peers, and management remains committed to its \$8bn expense target (requiring a \$600mn cost reduction ex-investment). We see ANZ's valuation as attractive at 14.3 times forward earnings, particularly relative to NAB and CBA (at 14.9 and 18.8 times respectively).

**Aristocrat Leisure (ALL)** – our investment thesis is premised on ALL's strong growth profile following the resolution of the COVID-19 crisis. ALL has a dominant position in Land Based Games (65% of EBIT) and is set to benefit from significant opportunities from Digital (35% of EBIT), which offers a wide range of outcomes. Lastly, the stock appears undervalued at 27.5 times forward earnings when considering the Industrials Ex-Financials Index trades at 28.2 times and ALL's superior long-term growth potential.

**BHP Group (BHP)** – we believe the company's valuation is attractive in the context of firm iron ore prices and China returning to production following COVID-19. BHP still trades on a 12-month forward P/E of 11.8 times, an EV/EBITDA of 5.4 times, and generates a FCF yield above 10%. Its balance sheet is robust (gearing ~15%), with management carrying out a well-defined capital allocation strategy. More broadly, we view BHP as a relatively defensive Metals & Mining exposure, with a diversified portfolio and clear strategy of capital allocation.

### Key Active Underweights

**National Australia Bank (NAB)** – we remain underweight the bank. While NAB has strengthened its capital position through a highly dilutive, discounted \$3.5bn capital raising and has increased collective provisioning, unlike its peers the bank is yet to recognise an AUSTRAC provision. Notwithstanding the improving trends for the bank, we see less scope for surplus capital compared to Westpac Bank (WBC) and ANZ Bank (ANZ). Further, both WBC and ANZ trade at more appealing valuations (at up to 10% discounts to NAB based on forward

earnings) and remain our preferred banking exposures at this time.

**CSL (CSL)** – we remain underweight CSL based on its forward valuation (40.3 times P/E and 27.1 times EV/EBITDA on a 12-month forward basis), which we believe appropriately captures the earnings outlook at this time. The growth outlook for CSL's key plasma products remains robust, with the company looking to further strengthen its relative market position through long-term investment in capacity, product innovation and collection centres.

**Wesfarmers (WES)** – our underweight position remains premised on the view its divisions, outside of Bunnings (62% of operating income), face significant earnings headwinds. Officeworks (5% of operating income) and the department store industry (including discount department stores Target and Kmart, 25% of EBIT) face increasing competition and excess physical store capacity. Furthermore, the company's Industrials segment (9% of EBIT) comprises cyclical, lower quality businesses. As such, we don't find the valuation attractive at 26.4 times forward earnings.

### Market outlook

The recovery in the Australian economy continues to exceed consensus expectations. The Australian economy contracted 2.5% in calendar 2020, however strong sequential growth in 2H2020 and positive momentum in early 2021 will see economic activity in 1Q2021 exceed pre-COVID levels.

The strength of the economic recovery is particularly evident via record levels for business conditions, business confidence and the strength in employment growth. The level of employment already exceeds pre-COVID levels, and after peaking at 7.5% in July 2020 the unemployment rate has declined sharply to 5.6% in March 2021.

Although wage rates remain subdued, the recovery in labour market income has been sufficient to offset the gradual withdrawal of temporary fiscal support. Moreover, the accumulation of \$125bn in excess household saving, in concert with strong asset price gains, leaves the consumer uniquely positioned to underpin economic growth in 2021-2022. Dwelling investment is set to provide solid support for economic growth over the next 18 months following a surge in demand for new housing construction, partly in response to the Government's Homebuilder subsidy. We expect the global economy to expand 6.5% and the Australian economy to expand 6% in 2021.

We continue to expect US inflation to surprise on the upside over the remainder of 2021 and for policy makers to resist pressure to normalise interest rates. This may see bond yields continue to rise at a moderate rate in coming months, however, we are cognisant that global business surveys will likely peak around mid-2021 which may limit the adjustment in bond yields, at least until the Federal Reserve signals it is preparing to taper its asset purchases. We do not expect this to happen until late 2021 at the earliest.

The A\$/US\$ should continue to be well supported by global reflationary forces, including robust commodity price trends. We continue to expect the A\$/US\$ to appreciate to the 81-83c range by the end of calendar 2021.

We are most overweight stocks within the Telecommunication Services, Media & Entertainment and Consumer Services sectors, and are underweight Real Estate, Consumer Staples and Financials.

## Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	12.43	4.09	8.34
Consumer Discretionary	9.89	7.88	2.01
Consumer Staples	1.44	4.99	-3.55
Energy	5.24	3.44	1.80
Financials	26.70	30.02	-3.32
Health Care	7.12	9.98	-2.86
Industrials	4.61	6.87	-2.27
Information Technology	4.58	4.23	0.34
Materials	21.12	20.62	0.50
Real Estate	2.90	6.62	-3.72
Utilities	2.89	1.26	1.63

## Top 5 holdings

	Portfolio %	Benchmark %	Active %
BHP	10.24	7.14	3.10
ANZ Banking	7.93	4.16	3.78
Westpac Banking	7.54	4.66	2.88
Commonwealth Bank of Australia	7.30	8.03	-0.72
Aristocrat Leisure	4.63	1.21	3.43

## Key active positions

Overweights	Portfolio %	Benchmark %	Active %
ANZ Banking	7.93	4.16	3.78
Aristocrat Leisure	4.63	1.21	3.43
BHP	10.24	7.14	3.10
Underweights			
National Australia Bank	0.00	4.47	-4.47
CSL	1.85	6.27	-4.42
Wesfarmers	0.00	3.12	-3.12

Portfolio holdings may not be representative of current or future investments. The securities discussed may not represent all of the portfolio's holdings and may represent only a small percentage of the strategy's portfolio holdings. Future portfolio holdings may not be profitable.

## Income and growth

	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.
Growth return	19.13	-5.60	-0.68	-1.17
Distribution return	15.06	11.43	8.58	8.37

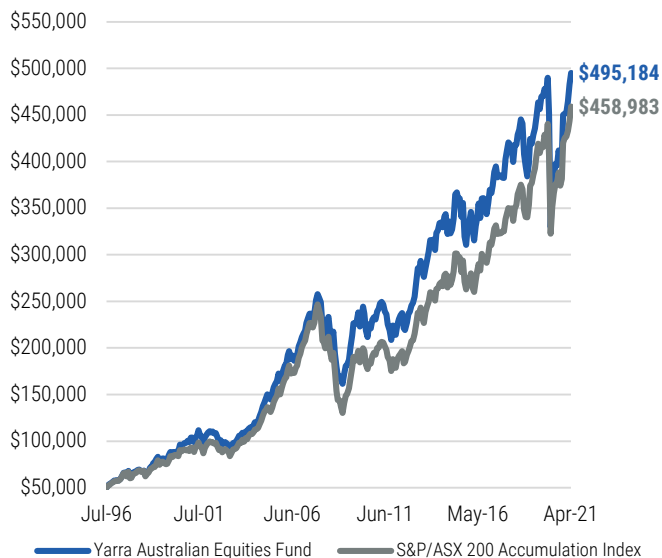
The Growth Return is measured by the movement in the Fund's unit price (inclusive of fees), ex-distribution, and can be positive or negative as the unit price can fluctuate with changes in the underlying market value of the Fund's assets. The Distribution Return is the amount that is paid to unitholders by way of income distribution in a 12-month period. It does not include capital distributions.

## Features

Investment objective	To achieve medium-to-long term capital growth through exposure to companies listed on the Australian Securities Exchange. In doing so, the aim is to outperform the S&P/ASX 200 Accumulation Index over rolling 3-year periods.	
Recommended investment time frame	5 - 7 + years	
Fund inception	July 1996	
Fund size	A\$123.0 mn as at 30 April 2021	
APIR codes	JBW0009AU	
Estimated management cost	0.90% p.a.	
Buy/sell spread	+/- 0.15%	
Platform availability	AMP Flexible Lifetime AMP PortfolioCare AMP Wealthview ANZ Grow Wrap Asgard BT Panorama BT Wrap Colonial FirstWrap Freedom of Choice Hub24 IOOF Pursuit Select	Macquarie Wrap Accumulator Macquarie Wrap Consolidator Netwealth North Oasis OnePath PortfolioOne PowerWrap SmartWrap Wealthtrac

## Investment performance comparison of \$50,000

After fees, since inception of the Yarra Australian Equities Fund, July 1996 to April 2021.



For illustrative purposes only. Past performance does not guarantee future results, which may vary. The total net fund returns shown are prepared on an exit to exit basis (i.e. they include all ongoing fees and expenses and assume reinvestment of all distributions). They do not take personal taxation into account. The comparison with the S&P/ASX 200 Accumulation Index is for comparative purposes only. Index returns do not allow for transactional, management, operational or tax costs. An index is not managed and investors cannot invest directly in an index. Note that the minimum initial investment amount for the Yarra Australian Equities Fund is \$10,000.

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## Applications and contacts

Investment into the Yarra Australian Equities Fund can be made by Australian and New Zealand resident investors only.

**Website** [www.yarracm.com](http://www.yarracm.com)

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