

Yarra Australian Equities Fund

Gross returns as at 31 January 2023

	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	5.84	9.64	11.88	5.90	7.23	8.68	10.59
S&P/ASX 200 Accumulation Index†	6.23	9.59	12.21	5.96	8.50	8.78	9.31
Excess return (before fees)‡	-0.39	0.06	-0.32	-0.06	-1.27	-0.10	1.28

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 31 January 2023

	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	5.76	9.40	10.88	4.96	6.25	7.68	9.59
S&P/ASX 200 Accumulation Index†	6.23	9.59	12.21	5.96	8.50	8.78	9.31
Excess return (after fees)‡	-0.47	-0.19	-1.32	-1.00	-2.25	-1.11	0.28

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

† 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.

‡ Excess return: The difference between the portfolio's return and the benchmark return.

Market review

The S&P/ASX 200 Accumulation Index returned +6.2% for the month, taking its 12-month return into positive territory of +12.2%. The broader ASX300 mirrored, gaining +6.3% for the month with global indices also strong (MSCI World Index +7.1%).

Most sectors delivered positive returns for the month, with Consumer Discretionary (+9.9%) the best performing sector, led by Aristocrat Leisure (ALL, +11.3%), JB Hi-Fi (JBH, +15.3%), Corporate Travel Management (CTD, +24.6%) reflective of resilient consumer spending patterns during the holiday season.

Within Materials (+8.9%), Metals and Mining produced some of the top performers for the month. Sandfire Resources (SFR, +14.9%), Northern Star Resources (NST, +15%) and Sims (SGM, +16.6%) all outperformed, with the gold price rising 3% to US\$1,928/oz and Copper rising ~10% over the month to close at US\$4.17/lb.

Conversely, the largest lagging sector was Utilities (-3.0%), following strong sector performance in the December quarter, with AGL Energy (AGL, -5.2%), Origin Energy (ORG, -3.2%) and APA Group (APA, -1.9%) all lower.

Portfolio review

Key Contributors

Reliance Worldwide (RWC, overweight) – the plumbing supplies company outperformed over the month of January following news of the widespread freeze event in the US in late December. These freeze events occur approximately every three years and this one should provide a solid boost to sales as repairs are undertaken to rectify frozen pipes. US 30-year mortgage rates also compressed ~50bps over the month, a positive move for home renovators that look to draw on their mortgages, with the share price also responding positively to this movement. Looking at the stock more broadly, the market is showing concern for a falling demand environment and RWC FY23 estimates were lowered after the company's August result and 1Q23 update. We believe RWC is a compelling opportunity with the market pricing for a significant decline in earnings (P/E of only 14 times vs 17 times mid cycle), while we remain constructive on the demand environment given the defensive nature of the majority of RWC's repair and remodelling sales.

Sandfire Resources (SFR, overweight) – the copper producer was a positive contributor to the portfolio. Copper prices increased ~10% over the month to close at US\$4.17/lb on expectations the re-opening of China post COVID-zero would

support copper demand. We like copper as a commodity given its leverage to electrification as a key material in batteries, transmission lines and electric motors. Following the company's recent equity raise, SFR is now better funded to complete the Motheo project in Namibia, and progress drilling activities to increase the mine life at the MATSA asset in Southern Spain. In our view, further de-risking of these projects, coupled with the outlook for copper markets, will continue to generate share price outperformance.

JB Hi-Fi (JBH, overweight) – the specialist retailer outperformed during the period, with the stock continuing to re-rate higher on a strong trading update and resilient consumer spending patterns. Both JB Hi-Fi and The Good Guys margins held up better than expected, with no evidence of a reversion to pre-COVID levels to date. We view JBH as a best-in-class operator that is well positioned to navigate the volatility ahead despite a softening consumer environment, with strong cash generation and a robust balance sheet. Unlike other COVID beneficiaries, consensus earnings already reflect a -30% earnings decline over the next three years, resulting in the company trading at a discount which we believe is unwarranted (8 times EV/EBIT vs 10 times long-term average).

Key Detractors

Incitec Pivot (IPL, overweight) – the explosives, fertilisers and industrial chemicals company underperformed over the month as ammonia prices reduced 23% to \$790/t. Ammonia prices in Europe have been falling with demand in Asia very soft, the removal of an 5.5% EU import duty & EU gas prices in late December at their lowest level for seven months. We note these movements are temporary rather than structural and note that spot prices are in line with consensus forecasts for FY23. We remain overweight the company, with positive catalysts on the horizon for the stock.

Origin Energy (ORG, overweight) – the energy retailer is under a takeover offer and lagged the market during the month, falling modestly despite an upgrade to full year earnings guidance for its Energy Markets business. The exclusive due diligence period with suitors Brookfield and EIG was extended again during the month, then ultimately lapsed without a binding bid materialising. The parties remain in talks, and we expect an update from the company imminently.

Macquarie Group (MQG, underweight) – performed strongly during the month on limited news flow, albeit continued volatility in US and European energy markets through their winter seasons should be positive for MQG's commodity business. We remain underweight the stock based on the view the recent earnings uplift is driven by its lower quality and highly cyclical businesses, which we see as unsustainable into the medium term.

Key Purchases

BHP Group (BHP) – we increased our position in the diversified miner during the period. We expect China's recent shift away from COVID-zero policies will continue to support commodity prices as industrial production and housing starts improve. With BHP progressing its planned takeover of OZL, copper will

represent more than a quarter of the company's revenue, a commodity we expect will outperform on supply challenges and increasing demand with China's reopening. However, we remain cautious on the outlook for iron ore prices that are already at unsustainably high levels, particularly considering recent price rallies. BHP's superior asset quality, strong cost control discipline, robust balance sheet, and well-defined capital allocation strategy are attractive, and support our preference for BHP over peers RIO, S32 and FMG.

Woodside Energy (WDS) – we have added to our position in Woodside. We are attracted to the energy company's strong growth profile that remains on budget and schedule to increase production by over 30% over the next two years. Sector leading exposure to short-term LNG prices should continue to support earnings, with global gas markets expected to remain short until after 2025 ahead of new project commissioning. While European winter conditions have proven to be mild, spot gas prices remain high, representing around 25% of the company's gas production. Recent 2023 company guidance is conservative in our view, and we point to two production upgrades during 2022 as evidence of upside risk to guidance across 2023.

Sims Metals (SGM) – we increased our position in the scrap and metals recycling company during the period. The company's US business, SA Recycling, is performing strongly and we see further upside from bolt-on acquisitions in this highly fragmented market. Scrap margins are improving following a period of significant moderation from historical highs and, in our view, are positioned to strengthen further. We believe Sims is trading close to trough earnings and represents attractive value at these levels. A skew towards improving environmental performance on increased capital spend in this area should position the business strongly relative to peers as environmental regulations tighten.

Key Sales

Evolution Mining (EVN) – we reduced our position in Evolution during the period. EVN has rallied nearly 85% following disappointing production levels, guidance downgrades and balance sheet concerns during the middle of 2022. We continue to see support for gold prices in the near to medium term, however at current prices we believe the turnaround story in EVN is now largely fully priced.

OZ Minerals (OZL) – we reduced our position in OZ Minerals during the period. With the \$28.25/share takeover bid from BHP supported by the OZL board, we see limited risk to deal completion at this stage. Copper prices increased ~10% over the month, however we see little likelihood of an increase in the bid given that the longer-term copper market fundamentals that support the bid remain largely unchanged. OZL is trading close to deal terms, as a result we see only limited potential for future outperformance.

TPG (TPG) – we reduced our position in TPG over the period following an adverse ACCC regulatory decision in December, which saw an outcome on the proposed network sharing agreement with Telstra (TLS) rejected. TPG has appealed the decision, though a ruling is not likely until the middle of this year. While headline price increases for Vodafone were

encouraging in an increasingly rational mobile market, we expect inflationary pressures, interest costs and balance sheet concerns to weigh on the near-term outlook.

Key Active Overweights

Reliance Worldwide (RWC) – the market is showing concern for a falling demand environment and RWC FY23 estimates were lowered after RWC's August result and 1Q23 update. We believe the plumbing supplies company is a compelling opportunity, with the market pricing for a significant decline in earnings (P/E of only 14 times vs 17 times mid cycle) while we remain constructive on the demand environment given the defensive nature of the majority of the company's repair and remodelling sales.

QBE Insurance Group (QBE) – the Australian insurer remains our preferred insurance exposure, which we expect will deliver strong earnings growth into 2023 and beyond driven by the earn through of strong volume growth, sustained rate growth and the beneficial impact of higher interest rates on investment earnings. QBE has substantially improved its underwriting discipline and product focus over the last five years, and we believe its 9.3 times FY23 earnings multiple excessively discounts the risks inherent in its business model.

Worley (WOR) – we remain overweight the professional project and asset services company. Following years of underinvestment in oil & gas projects, and with the more recent supply disruptions stemming from the war in Ukraine, expectations for project spend across WOR's traditional customer base has increased to 27% YoY growth. There is also a strong pipeline of margin accretive capital spend required to decarbonise energy production and provide more sustainable solutions across chemical and resources customers.

Key Active Underweights

CSL (CSL) – we remain underweight CSL based on the challenges the business faces returning to pre-COVID profitability (long-term quality and growth), coupled with its forward valuation (35.5 times P/E and 21.1 times EV/EBITDA on a 12-month forward basis), which we believe appropriately captures the earnings outlook at this time. While CSL is a key beneficiary of the post-COVID re-opening theme from a plasma collection perspective, we believe this is already reflected in consensus forecasts. However, in our view the prospect of higher costs going forward is underappreciated by the market, with donor fees and other collection centre costs likely to be higher for longer. We continue to prefer ResMed (RMD) within the Health Care sector, where we see better growth prospects.

National Australia Bank (NAB) – we remain underweight the bank due to our negative sector view. The favourable dynamics around expanding net interest margins (NIM) due to higher interest rates are now well understood, and we do not expect the gains to be sustained into the medium term. Further the banks are facing material earnings offsets through elevated expense growth and a normalization in bad debt expenses which will mean sector EPS is likely to be approaching peak levels. We hold small overweight positions

in Westpac Bank (WBC) and ANZ Bank (ANZ), where the valuations are more supportive at current levels.

Macquarie Group (MQG) – we remain underweight the stock based on the view the recent earnings uplift is driven by its lower quality and highly cyclical businesses, which we see as unsustainable into the medium term. We see significant downside risk to consensus forecasts beyond FY23, which currently reflects a strong contribution from lumpy items including gains on sale, performance fees and low loan-loss provisions. We do not expect growth in the more stable business to be able to offset this. As a result, we regard MQG's headline forecast P/E multiple of 15.0 times consensus forward earnings as unattractive.

Market outlook

Financial market enthusiasm at the commencement of 2023 has been stoked by three key forces; signs globally that the period of excess inflation is starting to recede, an acceleration in the trend decline in the US\$ which is helping to ease the contraction in global credit, and the expected impetus from "China's reopening" post is movement away from COVID zero. Each of these factors helps to diminish the risk of a harder landing for global growth and marginally increase the probability that a formal global recession may be avoided.

Importantly, the long-awaited pivot from major central banks appears to have been delayed until labour markets show more convincing signs of easing and the inflation down trend more assured. On balance, we still believe the US and Europe will enter a modest recession in 1H23 and inflation dynamics will change sufficiently for policy makers to conclude that the monetary policy is sufficiently restrictive to halt the tightening cycle in coming months.

We continue to argue that Australia presents as a safe haven from both the perspective of more robust growth relative to the G7 peer group and as having good leverage to signs of a trough in the economic cycle in China. Although both the RBA and we expect economic activity to slow significantly in 2023 to average just 1.5%, we believe Australia should be able to avoid a technical recession due to four key reasons:

1. Australia has been a net beneficiary of global commodity shortages. This surge in commodity prices saw Australia's export prices in A\$ terms move to their highest levels since the 1880s in 1H2022 and even though commodity prices are now off their peaks they remain very elevated from a historical perspective. The consequence has been strong national income growth, profits growth and an improving underlying fiscal position. Indeed, the Commonwealth Budget will likely be close to surplus for the 2023 financial year.
2. The household sector continues to hold a significant buffer of over \$270bn of excess savings relative to pre-COVID levels. Although we expect the impact of higher interest rates and higher living expenses will curtail consumer spending, we do expect the combination of rising wage growth and a run down in the level of savings to continue to support consumption spending.

3. Australia remains incredibly well placed to benefit from the global energy transition. Lithium is already a A\$10bn export industry for Australia and Australia is the world's dominant producer. Electric Vehicle sales are forecast to increase 10 times by 2030 and Australia has the world's 2nd largest copper resource. LNG is an important energy transition fuel, and currently accounting for 23% of global electricity generation. Australia just happens to be the world's equal largest exporter of LNG. Iron ore obviously remains Australia's biggest export and China the dominant customer. However, we expect the global energy transition to be steel intensive, opening up new customers.
4. Net migration into Australia contracted in 2021 for the first time since 1945. However, a very strong recovery was recorded through 2022 and a record level of net migration appears likely in coming months, ensuring that Australia's population growth will be close to 2% in 2023.

While the RBA has been later than most other developed nations in tightening policy, tighter financial conditions in 2022 have come via both significantly higher cash rates, higher government bond yields and wider corporate bond spreads. Following the February rate hike of 25 bps, we believe financial conditions are now in the restrictive zone and the RBA is now close to the finish of the tightening cycle. Nevertheless, following the February hike its clear the RBA is retaining the option of delivering two or more further rate hikes. From our perspective the RBA's focus on global growth, trends in household spending and the outlook for inflation and labour markets in informing their future decisions suggest that multiple additional hikes are unlikely to be required. Interest rate hikes in Australia will remain a month-to-month proposition for the next six months, however, our bias is that just one further 25 bps hike is likely to be delivered this cycle.

The A\$/US\$ has finally started to appreciate, after a long period of relative weakness. With Australia's external accounts remaining in excellent health, our expectation that Australia's economic growth will prove more robust and the prospect the US\$ down trend will persist as the Fed pivots from its aggressive hiking strategy, we expect the A\$/US\$ will appreciate to the mid-70s by mid-2023.

We are most overweight stocks within the Communication Services, Information Technology and Consumer Discretionary sectors and are underweight Financials, Real Estate and Health Care.

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	11.31	3.76	7.55
Consumer Discretionary	9.29	6.28	3.01
Consumer Staples	1.54	4.76	-3.22
Energy	6.91	5.94	0.98
Financials	21.21	28.42	-7.21
Health Care	4.44	9.66	-5.22
Industrials	6.29	5.66	0.63
Information Technology	9.13	2.66	6.47
Materials	24.86	25.38	-0.52
Real Estate	0.00	6.14	-6.14
Utilities	2.80	1.35	1.45

Top 5 holdings

	Portfolio %	Benchmark %	Active %
BHP	11.33	11.29	0.03
Commonwealth Bank of Australia	6.65	8.42	-1.77
Westpac Banking	5.27	3.75	1.52
Telstra	4.34	2.13	2.21
Woodside Energy	4.23	3.11	1.12

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
Reliance Worldwide	2.86	0.13	2.73
QBE Insurance	3.54	0.92	2.62
Worley	2.68	0.26	2.42
Underweights			
CSL	1.69	6.49	-4.80
National Australia Bank	0.00	4.53	-4.53
Macquarie Group	0.00	3.07	-3.07

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	-0.58	-8.64	-6.51	-2.13
Distribution return	11.46	13.59	12.77	9.81

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\$103.6 mn as at 31 January 2023	
APIR codes	JBW0009AU	
Estimated management cost	0.90% p.a.	
Buy/sell spread	+/- 0.15%	
Platform availability	Asgard Ausmaq BT Panorama BT Super Wrap FirstWrap GrowWrap	Hub24 IOOF Pursuit Macquarie Wrap Netwealth Oasis Powerwrap

Investment performance comparison of \$50,000

After fees, since inception of the Yarra Australian Equities Fund, July 1996 to January 2023.



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.

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

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