Yarra Australian Equities Fund

Gross returns as at 30 June 2022

	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	-8.40	-12.08	-6.58	3.30	5.52	9.19	10.12
S&P/ASX 200 Accumulation Index†	-8.77	-11.90	-6.47	3.34	6.82	9.29	8.88
Excess return (before fees)‡	0.37	-0.18	-0.12	-0.04	-1.30	-0.10	1.24

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 June 2022

	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	-8.46	-12.28	-7.42	2.37	4.56	8.17	9.13
S&P/ASX 200 Accumulation Index†	-8.77	-11.90	-6.47	3.34	6.82	9.29	8.88
Excess return (after fees)‡	0.31	-0.38	-0.95	-0.97	-2.27	-1.11	0.25

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

Australian equities declined sharply during the June quarter as Australia's first interest rate hike since 2010 pressured valuations, with only the Energy and Utilities sectors recording positive returns.

The S&P/ASX 200 Accumulation Index returned Index returned -11.9% for the quarter, taking its 12-month return to -6.5%. Globally, the MSCI World Index fell 14.2%. The ASX 200's forward P/E declined from 16.0 times to 12.5 times as the RBA lifted the official cash rate by 75 bps to 0.85%.

Within Energy (+1.5%), Woodside Energy (WDS, -0.8%) held value amid the global energy crisis given its relatively high exposure to the European gas market. Elsewhere, Worley (WOR, +10.3%) continued to rally amid growing demand for its engineering services in both oil & gas and sustainability projects, while oil refiner Ampol (+11.7%) benefited from the widening spread in the price of crude oil and petrol.

Within Utilities (+1.7%), AGL Energy (AGL, +6.9%) outperformed amid higher wholesale electricity prices, even as its proposed demerger (into coal generation and energy retailing businesses) was rejected by shareholders. Gas pipeline operator APA Group (APA, +8.2%) outperformed given its inflation-linked revenues and a renewed focus on its opportunities in the energy transition.

Conversely, the worst performing sectors included Consumer Discretionary (-14.9%) and Information Technology (-27.3%). In particular, JB Hi-Fi (JBH, -29.1%) and Nine Entertainment (NEC, -38.6%) declined in response to the deteriorating consumer environment, while Xero (XRO, -25.1%) delivered a disappointing full-year result and, as a high P/E firm, was pressured amid higher real rates.

Elsewhere, Real Estate (-17.8%) also experienced widespread declines given its negative correlation to higher rates, led by Charter Hall Group (CHC, -33.2%), Scentre Group (SCG, -15.1%) and Dexus (DXS, -16.6%).

Portfolio review

Key Contributors

Atlas Arteria (ALX, overweight) – the toll road operator outperformed due to its transparent inflation hedge and, moreover, as IFM's global infrastructure fund took a 14.96% stake in the company, causing speculation of a possible takeover bid. We maintain an overweight position based on ALX's strong liquidity and balance sheet position, discounted valuation and exposure to traffic recovery in Europe and the

US. ALX trades on less than 11.0 times normalised EV/EBITDA, which sufficiently captures the disruption from COVID-19 as travel restrictions and lockdowns reduce traffic volumes in the short term. Beyond traffic normalisation, we see a path towards value creation for ALX through concession extensions at APRR achieved as a means of funding expansion projects and settling the Dulles Greenway tolling regime.

Worley (WOR, overweight) – the engineering services firm outperformed due to expectations the global energy crisis will stimulate capex for both oil & gas and energy transition projects. We remain overweight the company. Following the Jacobs ECR acquisition, the business is diversified across different markets and is, in our view, well positioned to capture higher structural demand from energy transition work to low carbon solutions in addition to its traditional work for the oil & gas industry. We believe WOR's valuation provides significant support at current levels, with the stock trading on 18.9 times consensus forward earnings, a sharp discount to the Industrials ex-Financials at 25.5 times.

Amcor (AMC, overweight) – the plastic packaging company outperformed after announcing a stronger-than-expected trading update. Earnings per share in the third quarter came in at US20.4 cents per share, 4% above consensus and 13% above the prior year. Further, management upgraded full-year guidance for 9.5-11% EPS growth, above its prior guidance for 7-11%. The update supported our thesis for owning the stock. We view AMC as a defensive stock with a strong dividend yield (+4.0%) that should generate strong EPS growth in FY22 (+13%), before returning to more normal levels from FY23 onwards (mid-single digit). While AMC's Flexibles division faces volume headwinds as customers turn away from non-recyclable plastics, we believe the company is moving in the right direction from the point of view of producing more recycled product and using more post-consume resin. Further, shifts to higher margin customers (pharmaceutical and medical) and cost-out initiatives will provide an offset.

QBE Insurance (QBE, overweight) – the insurer outperformed amid stronger premium rate growth and higher future investment yield expectations as interest rates rose during the period. Our positive view towards the general insurer is premised on the company benefiting from an ongoing global hardening cycle in commercial insurance along with a return to unit growth after several years of volume declines as the company exited sub economic exposures. QBE's recent result demonstrated that the company has likely sufficiently strengthened reserves against problematic North American long tail insurance lines, which was previously viewed as a key risk. We continue to see upside to its relative valuation, with the stock trading on 10.4 times forward earnings and offering a 4.7% dividend yield.

Block (SQ2, underweight) – the digital payments company underperformed as the outlook for higher real rates pressured the tech sector's premium valuation. We are underweight on the grounds that its valuation (at a 12-month forward P/E of 50.4 times) more than captures the company's attractive growth outlook. In regard to Afterpay, we are negative on the BNPL industry given the prospect of heightened regulation (e.g. expense verification), increased competition, higher bad debts and the sustainability of current attractive margins.

Key Detractors

Tyro Payments (TYR, overweight) – the payment solutions provider underperformed as the outlook for higher real rates pressured the stock's valuation and, secondly, after the surprise departure of the chief executive. We remain overweight on the grounds that short-term headwinds (wage inflation, increased investment spending) are, in our view, more than reflected in TYR's valuation. As the lead provider of software that allows payment terminals to be integrated into point-of-sale (POS) systems, TYR remains in a defendable position versus peers such as the banks which rely on a clunky intermediary.

Northern Star (NST, underweight) – the gold miner underperformed alongside the gold price (-6% to $US1,817/oz) and in response to a disappointing 3Q22 result. While NST held FY22 guidance at 1.55-1.65mn ounces, it lifted all-in sustaining cost (AISC) guidance by $125/oz as it steps up development costs at its Pogo asset. We remain overweight the gold miner. We believe the company will benefit from higher-than-expected production and reserves/resource outcomes at its flagship KCGM SuperPit Mine, and we see the company's valuation as attractive at 3.7 times forward EV/EBITDA, which is only marginally above the wider Gold sector despite a superior growth outlook. More broadly, we have a selective exposure to the commodity, balancing the prospect of higher inflation with an uncertain rate hike path in the US (which is generally a headwind to the gold price).

CSL (CSL, underweight) – the blood plasma company outperformed as foot traffic continued to improve across its collection centres, with commentary suggesting that volumes are now broadly in line with pre-COVID levels. We remain underweight CSL based on its forward valuation (31.6 times P/E and 21.9 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, 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 and a strong competitive position versus peers.

Nine Entertainment (NEC, overweight) – the media company underperformed despite delivering a solid trading update during the period, with the market more focused on the deteriorating macro environment. Management expects FY22 EBITDA to be up 22% y/y, unchanged versus its previous guidance, supported by slightly stronger underlying metrics. Our positive view remains premised on a supportive valuation, its high-quality digital assets (Stan, 9Now and Domain), and a number of cost saving initiatives in the short term. We believe the ad market's recovery is only partially factored into NEC's valuation, with the stock trading at 9.1 times forward earnings. At these levels, we also do not believe sufficient value is

attributed to its subsidiaries when considering their long-term growth profile.

Link Administration (LNK, overweight) – the company underperformed over speculation the recent acquisition offer by Dye and Durham may not complete and after the ACCC temporarily suspended its approval timeline until it received further information. Subsequent to the ACCC's announcement, Dye and Durnham revised its takeover lower to $4.30 per share, which the Link board rejected but left the door open for negotiation. Notwithstanding the uncertainty, we remain overweight the stock. We see compelling value in its base share registry business and electronic conveyancing business PEXA, which has been supported by recent corporate interest. We hold a positive view of PEXA premised on its infrastructure-like characteristics of the property settlement exchange upon maturity, supplemented by numerous growth opportunities in immediate adjacencies. Further, LNK is positively leveraged to higher US interest rates, which we see as a meaningful tailwind over the medium term. Lastly, LNK trades at 15.0 times forward earnings, a discount to the Industrials ex-Financials at 21.8 times.

Key Purchases

Xero (XRO) – we initiated a position in the accounting software company during the period, taking advantage of recent underperformance. While consensus continues to view XRO as a subscriber growth story, we see significant upside from higher average revenue per user (ARPU) and expansion into financial services. Regarding financial services (i.e. invoicing, payments), early stage growth is positive and, we believe, could grow to around 50% of revenues in the next 5 years. For ARPU, we expect growth to materialise as a result of XRO' strategy to have an open platform, use M&A to purchase the most successful adjacent apps to bring into its platform, and justify price rises by including them into the core platform. Lastly, on valuation grounds subscriber total lifetime value (LTV) fell below 1.2 times and will be less than 1 times by FY23, thus the stock no longer requires an extended period of time to grow into the valuation.

Chalice Mining (CHN) – we established a position in the palladium project developer during the period. Following its announcement of a maiden Julimar Resource last year, CHN has, in our view, substantially de-risked its world-class project based in Western Australia. The project comprises one of the few, large scale and high-grade deposits of palladium-group metals outside of Russia, which historically produced around 40% of global palladium supply. In regard to the market more broadly, we acknowledge demand is set to weaken in the long term for its traditional use to make catalytic converters (and reduce emissions) for internal combustion engine (ICE) vehicles. However, palladium also has a unique ability to absorb hydrogen (can absorb >900-times its own volume under suitable conditions), providing a range of potential future facing demand applications.

The Lottery Corporation (TLC) – we increased our position in the company following its de-merger from Tabcorp (TAH). Our investment thesis is premised on Lotteries as having a defensive revenue stream, significant pricing power and growth opportunities driven by online penetration (which currently sits at 32%, below the global average of 50%). In particular, we see TLC as resilient in the current market environment, holding a strong market position in a heavily regulated industry with high barriers to entry. While TLC carries ESG risk as a gaming company, we view Lotteries as a low-risk part of the market given small average ticket sizes, limiting player harm, and we see TLC as a global leader relative to peers.

Key Sales

Ansell (ANN) – we exited our position in the company to reflect greater uncertainty around the outlook for earnings. In the short term, raw materials costs and slowing demand for its single-use/exam gloves (to pre-COVID levels) represent significant risk to consensus forecasts. In the medium to long term, the company has significant exposure to slowing global economic growth through its Industrials division. As a result, we no longer saw the company's valuation as attractive at a headline P/E of 12.0 times on a 12-month forward basis.

Metcash (MTS) – we exited our position in the wholesale distributor during the period after strong outperformance. Within Food & Liquor, we continue to see MTS as a beneficiary of higher inflation as the supermarket industry remains rational in passing through higher prices. However, we anticipate the softening macro environment in Australia may limit any further market share gains, with the "shop local" theme likely to dissipate as consumers search for value. Within Hardware (now 41% of group EBIT), we support management's store rollout and refurbishment strategy, but expect we expect this will be more than offset by Australia's slowing housing market. As a result, we no longer see MTS's headline valuation (at a 12-month forward P/E of 14.2 times) as attractive given the risk to earnings as the cycle persists.

Amcor (AMC) – we reduced our position in the plastic packaging company during the period following strong outperformance, but remain overweight. We view AMC as a defensive stock with a strong dividend yield (+4.0%) that should generate strong EPS growth in FY22 (+13%), before returning to more normal levels from FY23 onwards (mid-single digit). While AMC's Flexibles division faces volume headwinds as customers turn away from non-recyclable plastics, we believe the company is moving in the right direction from the point of view of producing more recycled product and using more post-consume resin. Further, shifts to higher margin customers (pharmaceutical and medical) and cost-out initiatives will provide an offset.

Key Active Overweights

Link Group (LNK) – we are positive on the company because we see compelling value in its base share registry business and electronic conveyancing business PEXA, which has been supported by recent corporate interest. We hold a positive view of PEXA premised on its infrastructure-like characteristics of the property settlement exchange upon maturity, supplemented by numerous growth opportunities in immediate adjacencies. Further, LNK is positively leveraged to higher US interest rates, which we see as a meaningful tailwind over the medium term. Lastly, LNK trades at 15.0

times forward earnings, a discount to the Industrials ex-Financials at 21.8 times.

Worley (WOR) – we believe the company is in a strong position to benefit from the recovery in its traditional work and, increasingly, new sustainability projects. Following the Jacobs ECR acquisition, the business is diversified across different markets and is well positioned to capture higher structural demand from energy transition work to low carbon solutions. We believe WOR's valuation provides significant support at current levels, with the stock trading on 17.9 times consensus forward earnings, a sharp discount to the Industrials ex-Financials at 21.8 times.

Aristocrat Leisure (ALL) – our positive investment view remains premised on ALL's dominant position in Land-Based Games and significant opportunities from Digital, which likely offers a wide range of outcomes. We see the disruption from its exposure to Ukraine as temporary. Around 1,000 (40%) of its employees within the Digital business work in Ukraine, most of whom have now moved to safer regions of the country or to Poland. We see ALL's valuation as undervalued at 18.7 times forward earnings when considering the Industrials Ex-Financials trades at 23.3 times and ALL's superior long-term growth potential.

Atlas Arteria (ALX) – we maintain a high-conviction overweight position based on ALX's strong liquidity and balance sheet position, discounted valuation and exposure to traffic recovery in Europe and the US. ALX trades on less than 11.0 times normalised EV/EBITDA, which sufficiently captures the disruption from COVID-19 as travel restrictions and lockdowns reduce traffic volumes in the short term. Beyond traffic normalisation, we see a path towards value creation for ALX through concession extensions at APRR achieved as a means of funding expansion projects and settling the Dulles Greenway tolling regime. M&A risk, expressed in the period, suggests scope for the value gap to be closed on a shorter time frame.

TPG Telecom (TPG) – our thesis is premised on the improving outlook for the mobiles market, recovery in volumes post COVID and 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 new products such as Fixed Wireless.

Key Active Underweights

CSL (CSL) – we remain underweight CSL based on the challenge the business faces returning to pre-COVID profitability, coupled with its forward valuation (31.6 times P/E and 21.9 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 blood 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 center costs likely to be higher for longer. We continue to prefer ResMed (RMD) within the Health Care sector, where we see better growth prospects and a strong competitive position versus peers.

National Australia Bank (NAB) – we remain underweight the bank, due to our negative sector view, following recent outperformance. Favourable dynamics of excess provisions and capital are now well understood, while low bad debts and significant buybacks have seen the sector re-rate to trade at peak multiples versus pre-provision earnings. We believe consensus estimates for pre-provision forecasts are too high in the absence of revenue growth – with earnings quality deteriorating in recent years as abnormal items take up a larger proportion – and an inability for the industry to meaningfully take costs out. 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 FY22, which currently reflects a strong contribution from lumpy items including gains on sale, performance fees and low loan-loss provisions. Meanwhile, 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 15.3 times consensus forward earnings as unattractive.

Wesfarmers (WES) – our underweight position remains premised on the view its divisions, outside Bunnings (62% of operating income) which we expect will also slow as the housing market correction persists, face significant earnings headwinds. In particular, 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. As such, we don't find the valuation attractive at 24.0 times forward earnings.

Transurban (TCL) – while we continue to believe TCL has a strong growth outlook (with a number of new projects and expansion plans), we see its risk-adjusted total return potential as less attractive in the current macro environment. Our preferred toll road exposure is Atlas Arteria (ALX), where we see greater valuation support particularly through concession extensions at APRR and settling the Dulles Greenway tolling regime.

Market outlook

Geopolitical events and surging commodity prices have taken centre stage in 2022, shaking risk sentiment and challenging consensus' optimistic forecast for global growth. From our perspective, although for the past six months our forecasts for global growth in 2022 have been below consensus, we believe a series of downgrades will soon be evident for global earnings growth in most major markets. Surging commodity prices and ongoing supply shortages have resulted in further upside to the inflation outlook and risks forcing the hand of central banks in coming months to try to contain rising inflation

expectations. The reality for 2022 is likely a world of higher inflation, slower growth and higher financing costs awaits.

Australia does have some key natural advantages in such a climate. The most notable is that Australia's export dominance of iron ore, coal, LNG, gold, wheat and base metals contribute close to 80% of Australia's exports and each of these commodities have seen strong price rises in 1H 2022 which will translate into a large positive national income boost even if spot prices retreat in coming weeks. Indeed, Australia presents as a safe haven market which is far from the conflict in Europe, an exporter of in demand raw materials and given its own undershooting of its inflation target since 2015 it has ample room to adjust policy settings at a gradual pace.

Australia also has the benefit of recovering underlying household income growth, $230bn in 'excess saving', strong corporate profit growth, robust capex expectations in concert and improving government finances which suggests Australian economic growth in 2022 will remain more robust than its developed economy peer group. In CY2022 we expect the Australian economy to expand at an above 'potential' rate of 3%. While this is slower than the 4% pace recorded in 2021 it is still sufficient to see further employment growth gains and we expect the unemployment rate will soon fall below 4% and below the RBA's estimate of non-accelerating inflation rate of unemployment (NAIRU) and further wage pressure will become evident into mid-2022.

While the RBA has been later than most other developed nations in tightening policy, tighter financial conditions in 2022 are likely to come via both significantly higher cash rates and a stronger currency. The A$/US$ has in recent months been buffeted by concerns of a peak in global industrial growth indicators and slowing China economic momentum. Nevertheless, Australia's external accounts are in their best position since the early 1970s and surging commodity prices in early 2022 is providing an incentive for the A$/US$ to commence an appreciation cycle, together with the attractive carry on offer. We expect the A$ will finish 2022 at around 76 cents, albeit the risk to this forecast is on the upside.

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

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	12.59	4.06	8.52
Consumer Discretionary	10.29	6.39	3.89
Consumer Staples	0.00	5.26	-5.26
Energy	7.67	5.91	1.76
Financials	21.57	27.93	-6.37
Health Care	4.58	10.17	-5.59
Industrials	7.33	6.00	1.33
Information Technology	8.45	2.74	5.71
Materials	23.84	23.71	0.12
Real Estate	0.00	6.33	-6.33
Utilities	2.22	1.49	0.72

Top 5 holdings

	Portfolio %	Benchmark %	Active %
BHP	10.43	10.78	-0.36
Commonwealth Bank of Australia	6.59	7.96	-1.38
Westpac Banking	5.22	3.52	1.69
Woodside Energy	4.37	3.10	1.27
Telstra	4.31	2.31	2.01

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
Link Administration	3.26	0.10	3.16
Worley	3.30	0.27	3.03
Aristocrat Leisure	4.18	1.19	2.99
Underweights			
CSL	1.84	6.69	-4.86
National Australia Bank	0.00	4.55	-4.55
Macquarie Group	0.00	3.06	-3.06

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	-16.77	-10.82	-8.00	-1.60
Distribution return	9.35	13.19	12.55	9.77

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$95.4 mn as at 30 June 2022	
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 June 2022.

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.

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Disclaimers

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