

Yarra Emerging Leaders Fund

Gross returns as at 31 January 2022

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception* % p.a.
Yarra Emerging Leaders Fund	-7.86	-3.73	12.67	12.99	11.61	12.83	11.50
Emerging Leaders Combined Benchmark†	-8.84	-5.85	9.34	12.46	10.99	9.42	7.47
Excess return (before fees)‡	0.98	2.12	3.33	0.53	0.62	3.41	4.04

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 management costs, meaning they do not reflect the deduction of any investment management fees and expenses 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 2022

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception* % p.a.
Yarra Emerging Leaders Fund	-7.96	-4.03	11.28	11.59	10.24	11.44	10.20
Emerging Leaders Combined Benchmark†	-8.84	-5.85	9.34	12.46	10.99	9.42	7.47
Excess return (after fees)‡	0.88	1.82	1.94	-0.87	-0.76	2.02	2.73

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 Emerging Leaders Fund: September 1997

† Comprising 50% S&P/ASX Midcap 50 Accumulation Index and 50% S&P/ASX Small Ordinaries Accumulation Index

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

Market review

Australian equities declined sharply in January as high inflation spurred Federal Banks to accelerate quantitative tapering and signal earlier rate rises.

The Emerging Leaders Benchmark declined 8.8% during the month, underperforming the broader ASX300's -6.5% return and taking its 12-month return to +9.4%. Globally, the S&P500 and MSCI World Index returned -5.2% and -4.9% respectively as US real yields rose, with the US 10-year Treasury Inflation-Protected Securities (TIPS) climbing 38 bps to -0.69% as the US Fed said it would likely start to increase interest rates in March.

At a sector level, high-PE cohorts within Health Care (-16.7%) and Information Technology (-14.9%) recorded the most significant declines, led by companies with long-dated cash flows like Wisetech Global (WTC, -22.7%), Altium (-21.0%) and Pro Medicus (PME, -27.8%). Gold (-13.7%) also declined significantly given its negative correlation with real interest rates.

Conversely, Energy (-0.7%) was the strongest performer as Brent Crude lifted by 18% to US\$92/bbl. Oil & Gas producer Beach Energy (BPT, +17.5%) and engineering services company Worley (WOR, +8.7%) were among the top performers. Utilities (+7.7%) also outperformed during the

period amid the outlook for higher electricity prices, supported by AGL Energy (AGL, +15.6%).

Portfolio review

Key Contributors

IGO Limited (IGO, overweight) – the EV commodities miner outperformed alongside the lithium price, with spodumene rising 6% to US\$2,710/t. Our positive thesis remains premised on the miner's recent US\$1.4bn Greenbushes acquisition, its A\$1.1bn takeover of nickel miner Western Areas (WSA) and its existing portfolio of high-quality assets. We support the Greenbushes 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 support the WSA acquisition on the grounds it diversifies production (rebalancing commodity exposure to 70% Li, 30% Ni) and extends the mine life for nickel production (which is currently through its world-class Nova asset).

Worley (WOR, overweight) – the engineering services company outperformed as oil prices increased, with Brent Crude rising 18% to US\$92/bbl during the period. We remain overweight WOR, which we believe is in a strong position to withstand a lower-than-expected recovery in its traditional work. 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 16.5 times forward earnings, a sharp discount to the Industrials ex-Financials at 24.7 times.

TPG Telecom (TPG, overweight) – the telco held its value during the period without any material news, outperforming the declining market. 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 Detractors

Megaport (MP1, overweight) – the company underperformed after giving a 2Q22 update which revealed higher costs as the business adjusts its operating model to focus on its indirect sales channel. We view the pick-up in costs as supporting an acceleration in executing on the growth opportunity and remain overweight the stock, premised on strong growth from the core business connecting data centres to the cloud, with a strong pipeline in its key US geography as businesses invest in IT projects. With its expansion into telecommunication services – which leverages the same infrastructure – the total addressable market more than doubles. While the company is currently at an inflection point for earnings and cashflow we believe it will turn positive in the next year. We do not believe MP1's strong and sustainable revenue growth outlook is reflected in its share price.

Nanosonics (NAN, overweight) – the disinfection medical device maker underperformed during the period without any company-specific news. Our positive view towards the company remains premised on its leverage to the re-opening US economy and, moreover, the growing acceptance of its proprietary product, translating into higher earnings growth. NAN's product, Trophon, is the global market leader with over 50% market share in North America. As regulatory change relating to disinfection protocols continues to drive adoption of NAN's products, the sale of consumables for its devices generates a high-quality, annuity-style revenue stream. NAN also has a strong balance sheet – it is in a net cash position – to fund future growth and support ongoing product innovation.

Pinnacle Investment Management (PNI, overweight) – while the investment manager didn't announce any news during the period, the stock declined alongside equity markets. We

continue to see PNI as a high-quality company with further upside potential on a three-year view. The asset manager now trades at a 12-month forward P/E of 23.1 times, which partially factors in its superior growth versus the wider sector and the high level of growth investment captured in earnings. In the long term we continue to expect new strategies and managers, as well as underlying growth in existing managers, to drive double digit earnings growth.

Key Purchases

Sandfire Resources (SFR) – we increased our position in the copper producer during the period. We view the announced MATSA acquisition as a high-quality, low-cost operation, comprising three underground mines in Spain that produce mostly copper and zinc and a processing plant with capacity of 4.7mtpa. Importantly, the purchase extends SFR's mine life across its operations and resolves the looming earnings hole in FY23 as SFR's main existing asset, Degruusa, ceases operating. Lastly, we view SFR's valuation as attractive at a 12-month forward EV/EBITDA of 4.0 times, well below peer OZ Minerals (OZL) at 7.0 times.

Kelsian (KLS) – we increased our position in the travel services company based on our positive view of its Transit Systems (80% of expected EBITDA) business, which has long-term contracts with governments or agencies to operate bus services and limited impact from reduced service frequency. The business has opportunities for a large pipeline of government contracts. We also see upside from demand recovering for domestic tourism, which in our view will generate volume and yield growth, translating into high organic earnings growth.

Evolution Mining (EVN) – we increased our position in the gold miner during the period. EVN is our preferred exposure within the S&P/ASX Midcap 50 Index, based on its diversified, high-quality assets and strong management team. While the growth outlook may not be as compelling as peer Northern Star (NST), we see upside based on the company's production at Cowal and Red Lake assets and improving cost profile.

Key Sales

Regis Resources (RRL) – we exited our position in the gold miner during the period. Following the latest FY22 guidance downgrade, we have lower confidence in its operational performance for existing assets. Further, we expect any relative upside potential would only materialize in the regulatory approval for the McPhillamys project, which is unpredictable and, if successful, would likely require additional equity (estimated at \$400-500mn) for development. As a result, we no longer see RRL's headline valuation multiple (at a forward EV/EBITDA of 3.1 times) as attractive.

Iluka Resources (ILU) – we reduced our position during the period, moving from overweight to underweight. We are cautious about the company's operating outlook as developments in China's real estate industry slows from elevated levels, which we believe is not fully reflected

despite its headline valuation multiple (forward EV/EBITDA of 5.0 times). We regard the industry structure as attractive (consolidated supply), with less pricing volatility compared to previous cycles. Our preferred mining exposures include IGO Limited (IGO) and Alumina (AWC).

Aventus Group (AVN) – we reduced our position in the large format retail REIT following recent outperformance and, secondly, as the proposed merger with HomeCo Daily Needs REIT raises governance concerns with the stock. While we continue to view the merged entity favourably compared to shopping mall peers, with 'essential services' making up significantly more NOI, we are concerned about the external management structure. We believe this leads to inherent conflict and an ESG discount relative to internally managed peers.

Key Active Overweights

IGO Limited (IGO) – our positive thesis is premised on the miner's recent US\$1.4bn Greenbushes acquisition, its A\$1.1bn takeover of nickel miner Western Areas (WSA) and its existing portfolio of high-quality assets. We support the Greenbushes 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 support the WSA acquisition on the grounds it diversifies production (rebalancing commodity exposure to 70% Li, 30% Ni) and extends the mine life for nickel production (which is currently through its world-class Nova asset).

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 23.2 times forward earnings, a discount to the Industrials ex-Financials at 24.7 times.

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 on less than 11.0 times normalised EV/EBITDA, which more than 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.

Key Active Underweights

Mineral Resources (MIN) – we remain underweight based on the view the positive outlook is fully priced in at current levels. And while MIN's Wodgina lithium project is well positioned to benefit from higher lithium prices as the EV thematic accelerates, its iron ore business is exposed to downside risk based on unsustainably high iron ore prices (which have already fallen to <US\$130 per tonne from recent peaks) into the medium term.

Bluescope Steel (BSL) – our underweight position is premised on our view the current favourable conditions are unsustainable in the medium term, with steel prices likely to revert and housing volumes likely to normalise. As a result, its headline forward P/E of 4.5 times is misleading. That being said, we continue to view BSL as a high-quality cyclical company with attractive assets (both domestically and internationally) and a strong balance sheet.

Pilbara Minerals (PLS) – while we hold a positive view towards the company as commercial production ramps up at its flagship Pilgangoora project our preferred EV commodity exposure is IGO Limited (IGO). Our positive thesis on IGO is premised on the miner's recent US\$1.4bn Greenbushes acquisition, its A\$1.1bn takeover of nickel miner Western Areas (WSA) and its existing portfolio of high-quality assets.

Market outlook

The pattern of quarterly economic growth in Australia remains volatile, having declined 1.7% (q/q) in 3Q under the impact of the Delta strain of COVID. Nevertheless, record fiscal stimulus and easy financial conditions have helped underpin solid real economic growth of 3.9% (y/y) and a 4Q recovery from the Delta variant disruption is expected to see real economic growth in calendar 2021 to average 4.0%.

Recovering underlying household income growth, \$200bn in 'excess saving', strong corporate profit growth, low inventory levels and robust capex expectations – in concert with a still solid global growth backdrop – suggests Australian economic growth into 2022 will be above 'potential'. In both CY2022 and CY2023 we expect the Australian economy to expand at an above 'potential' rate of 3%.

The strength of the economic recovery has been particularly evident via the strength in employment. After peaking at 7.5% in July 2020, the unemployment rate has declined sharply to 4.2% in December 2021. In essence the unemployment rate is now in line with the RBA estimate of non-accelerating inflation rate of unemployment (NAIRU) and the combination of excess demand relative to available supply has seen 2H21 produce sufficient broad based inflation pressures to prompt an abrupt reassessment of the RBA's monetary stance. We expect the RBA will commence increasing interest rates in 4Q2022 with a 35 bps hike, with a further four 25 bps rate hikes in 2023.

Although we remain constructive on global economic growth, we believe the industrial cycle peaked in mid-2022

and that a relatively controlled slowing in economic activity is currently taking place. Nevertheless, there are some areas that are cause for concern. For over 18 months we have warned about rising US inflation pressures and rising inflation expectations, and while these threats have been realised, supply chain constraints and energy shortages in the Northern Hemisphere risk inflation pressures becoming more widespread and more entrenched. With the peak in global business surveys having passed, cost inflation continuing to escalate and the Federal Reserve announcing its decision to taper bond purchases, we expect bond yields will move higher, providing some ongoing challenges for risk assets.

The A\$/US\$ has recently been buffeted by concerns of a peak in global industrial growth indicators, slowing China economic momentum and volatility in commodity prices. Nevertheless, Australia's external accounts are in their best position since the early 1970s and despite some moderation in commodity prices the A\$/US\$ should remain supported by the RBA joining other central banks in tightening interest rates this year. We expect the A\$ will finish CY 2022 at around 76 cents.

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

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	12.68	7.82	4.86
Consumer Discretionary	10.08	12.60	-2.52
Consumer Staples	3.95	3.80	0.16
Energy	3.38	5.71	-2.33
Financials	6.54	10.11	-3.57
Health Care	10.31	4.36	5.95
Industrials	7.93	10.65	-2.72
Information Technology	10.01	8.05	1.96
Materials	24.43	25.11	-0.68
Real Estate	5.52	10.03	-4.52
Utilities	0.00	1.75	-1.75

Top 5 holdings

	Portfolio %	Benchmark %	Active %
IGO	5.75	1.43	4.31
Link Administration	4.61	0.54	4.07
Atlas Arteria	4.07	1.13	2.94
OZ Minerals	3.55	1.46	2.09
Carsales.com	3.52	1.13	2.40

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
IGO	5.75	1.43	4.31
Link Administration	4.61	0.54	4.07
Atlas Arteria	4.07	1.13	2.94
Underweights			
Mineral Resources	0.00	1.67	-1.67
Bluescope Steel	0.00	1.65	-1.65
Pilbara Minerals	0.00	1.50	-1.50

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	9.93	10.05	8.46	9.23
Distribution return	1.34	1.55	1.77	2.21

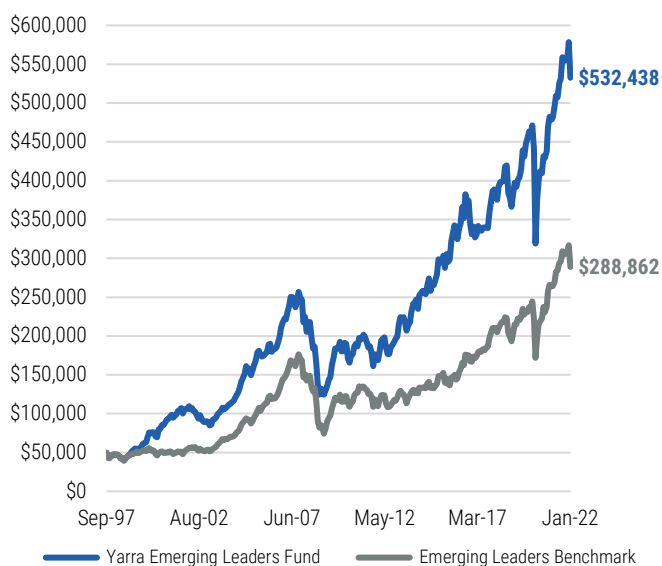
The Growth Return is measured by the movement in the Fund's unit price (inclusive of fees), ex-distribution, and can be positive or negative as the unit price can fluctuate with changes in the underlying market value of the Fund's assets. The Distribution Return is the amount that is paid to unitholders 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 small and medium sized Australian companies that are considered to possess strong capital growth potential. In doing so, the aim is to outperform the benchmark over rolling 3-year periods.	
Recommended investment time frame	5 - 7 + years	
Fund inception	September 1997	
Fund size	A\$55.8 mn as at 31 January 2022	
APIR codes	JBW0010AU	
Estimated management cost	1.25% p.a.	
Buy/sell spread	+/- 0.20%	
Platform availability	Asgard BT Panorama Hub24 Macquarie Wrap	Mason Stevens MLC Navigator MLC Wrap Praemium

Investment performance comparison of \$50,000

After fees, since inception of the Yarra Emerging Leaders Fund, September 1997 to January 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 benchmark (comprising 50% S&P/ASX Midcap 50 Accumulation Index and 50% S&P/ASX Small Ordinaries 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.

Applications and contacts

Investment into the Yarra Emerging Leaders Fund can be made by Australian resident investors only.

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Disclaimers

The Yarra Emerging Leaders Fund is substantially invested in the Yarra Emerging Leaders Pooled Fund ('Pooled Fund'). References in this document to the underlying assets or investments of the Fund generally relate to the assets held in the Pooled Fund. The Fund's benchmark comprises 50% S&P/ASX Midcap 50 Accumulation Index and 50% S&P/ASX Small Ordinaries Accumulation Index.

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