



# UBS Microcap Fund

July 2021

## Fund description

The Fund is an actively managed fund investing in a portfolio of 35 to 65 predominantly Australian Microcap equity securities across a range on industry sectors.

## Investment return objective

The Fund aims to outperform (after management costs) the S&P/ASX Small Ordinaries Accumulation Index over rolling five year periods.

## Active security positions

Overweight	Underweight
Mainstream	Iluka Resources
Empired	Pilbara Minerals
RPMGlobal	Steadfast Group
EROAD	Seven Group
Pacific Smiles	ARB Corporation

## Active industry positions

Overweight	Underweight
Software & Services	Materials
Capital Goods	Real Estate
Health Care Equipment & Services	Consumer Services
Technology Hardware & Equipment	Energy
Commercial & Professional Services	Food Beverage & Tobacco

## Investment Strategy

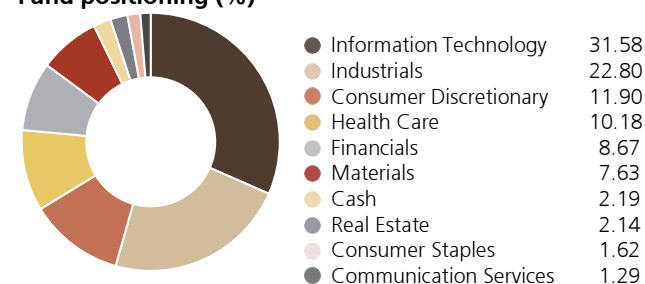
The Portfolio Manager's overarching strategy is to identify those Microcap shares that are believed to be undervalued by the market, based on an assessment of the companies' future cash flows. Normally the Fund will hold between 35–65 stocks in companies with a market capitalisation of generally less than \$250m at the time of initial purchase. The Portfolio Manager searches for businesses that have exposure to growing markets or are benefiting from changes in market structure and are in a rapid growth phase of their life cycle.

## Fund information

Inception date	12 August 2014
Fund size	\$ 53.8 m
Management fee	1.20% pa
Performance fee*	Yes
Minimum initial investment	\$10,000 (via mFund and online application \$5,000)
Typical number of holdings	35 to 65
Distributions	Semi-annually
Buy/sell spread	+/- 0.70%
APIR code	UBS0057AU
mFund code	UAM02

\* The performance fee equals 20% of the amount by which the Fund outperforms the S&P/ASX Small Ordinaries Accumulation Index.

## Fund positioning (%)



## Investment performance

Fund	1 month %	3 months %	1 year %	3 years % pa	5 years % pa	Since inception* % pa
Total return	2.14	5.07	54.24	18.39	15.64	17.11
Benchmark**	0.68	4.06	32.30	9.21	9.57	9.62
<b>Added Value</b>	<b>1.46</b>	<b>1.01</b>	<b>21.94</b>	<b>9.18</b>	<b>6.07</b>	<b>7.49</b>

\*Inception date: 12 August 2014. \*\*S&P/ASX Small Ordinaries Accumulation Index.

Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.

## Portfolio review

After fees and expenses, the Portfolio increased by 2.14% during the month, outperforming its benchmark by 146 bps.

Positive contributors included Empired, Envirosuite and RPM Global. IT services provider Empired outperformed after receiving a takeover offer pitched at a 64% premium from French multinational Capgemini. Envirosuite rose following a solid Q4 update and the completion of its recent capital raising. New management's focused strategy, balance sheet flexibility and a significant market opportunity provide reason for optimism. RPM provided an update on year-end software sales, delivering a solid outcome which showed good closing momentum from its prior update in mid-June. Software subscription total contract value of \$47.7m represented solid growth from pcp (\$34.5m).

Negative contributors included Pilbara Minerals (not held), Urbanise and Pacific Smiles. Pilbara Minerals (not held) rose strongly on continued momentum in the lithium price and outlook for the Electric Vehicle industry. Urbanise was lower following recent outperformance, with its Q4 update highlighting 19% growth in revenue for the year as the company moves closer to cashflow breakeven. Pacific Smiles was weaker reflecting investor concern about the impact of lockdowns on its dental network.

## Market Review

Australian shares rose modestly in July despite ongoing lockdowns across the east coast of the country. The S&P/ASX Small Ordinaries Accumulation Index returned 0.7% for the month, taking its 12-month return to 32.3%. However, the market lagged overseas indices, with the S&P500 returning 2.4% during the month amid an upbeat US corporate earnings season.

Metals & Mining ex-Gold (+10.2%) was the top contributor to the index, supported in most part by miners leveraged to the electric vehicle theme, including Pilbara Minerals (PLS, +22.1%), Orocobre (ORE, +27.5%) and Galaxy Resources (GXY, +27.0%).

Corporate activity increased across the broader market during the period. Within the Small Ords, Australian Pharmaceutical Industries (API, +26.5%) received a takeover bid from Wesfarmers (WES) at \$1.38 per share (all-cash), a 21% premium to its last-traded share price prior to the announcement.

Conversely, sectors leveraged to the re-opening theme underperformed during the period. Underperformers included Consumer Services (-3.1%), Media & Entertainment (-3.8%) and Retailing (-3.2%). At a stock level, Marley Spoon (MMM, -30.7%) was the worst performer after delivering a disappointing market update, with sales unable to match high growth in the pcp and costs elevated due to labour shortages and supply chain disruptions.

## Outlook

The Australian economy completed 1H2021 with strong momentum, prompting the RBA and consensus to upgrade expectations for both 2021 and 2022 calendar year growth. Both the size of the economy and people employed comfortably exceed pre-pandemic levels. The unemployment rate declining from a peak of 7.5% in July 2020 to just 4.9% in June 2021 is the clear highlight. Nevertheless, renewed COVID-related lockdowns in Melbourne, Sydney and South East Queensland will sharply impact the data in 3Q21 and materially alter our growth forecasts for the remainder of 2021 and 2022.

We believe the interruption to economic growth from renewed lockdowns will be an aberration within an improving trend rather than a view altering event. Indeed, the fundamentals that will drive the economic recovery remain in place. The recovery in labour market income has been sufficient to offset the gradual withdrawal of temporary fiscal support. Moreover, the accumulation of an estimated \$171bn in excess household saving, in concert with strong asset price gains, leaves the consumer uniquely positioned to underpin economic growth in 2021-22. Dwelling investment is set to provide solid support for economic growth over the next 12 months following a surge in demand for new housing construction, and a broader-based lift in business investment expectations is an important step in ensuring a sustained economic recovery. We expect the global economy to expand 6.5% and the Australian economy to expand 4.75% in 2021, a downward revision from our pre-lockdown forecast of 6%. We expect another strong year of economic growth in 2022 of 4.0%.

While we continue to expect US inflation to surprise on the upside over the remainder of 2021, the biggest inflation surprises are now behind us, and our expectation that global business surveys would likely peak around mid-2021 appears to have been realised. The peak in global business surveys, in concert with slower bond issuance relative to central bank buying, helped push real bond yields to record lows over recent weeks. As the Federal Reserve signals increased willingness to taper its purchases, and global economic and inflation indicators remain elevated, we expect bond yields will again start to move higher through the remainder of 2021. We expect US 10 year yields to approach 1.80% by the end of 2021.

The A\$/US\$ has recently been buffeted by concerns of peak in global industrial growth indicators, slowing China economic momentum and recent declines in iron ore 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 global reflationary forces through 2021-22. Reflecting the factors above, we have lowered our expectations for the A\$/US\$ somewhat over the remainder of 2021 and now expect the A\$/US\$ to finish the year in the 76-78c range, down from a forecast 81-83c range previously.

## Client Services

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