

UBS Yarra Australian Share Fund

August 2021

Fund description

The Fund is an actively managed fund investing in a portfolio of 30–70 listed Australian equity securities listed on the Australian Securities exchange.

Investment return objective

The Fund aims to outperform (after management costs) the S&P/ASX 300 Accumulation Index over rolling five year periods.

Active security positions

Overweight	Underweight
Australia and NZ Banking	National Australia Bank
Aristocrat Leisure	CSL
Westpac Banking	Wesfarmers
ResMed	Macquarie Group
Telstra Corporation	Woolworths Group

Active industry positions

Overweight	Underweight
Media & Entertainment	Real Estate
Telecommunication Services	Pharmaceuticals Biotechnology & Life Sciences
Consumer Services	Diversified Financials
Transportation	Food & Staples Retailing
Software & Services	Commercial & Prof Services

Investment performance

Fund	1 month %	3 months %	1 year %	3 years % pa	5 years % pa	Since inception* % pa
Total return	2.15	5.27	29.68	7.44	7.63	9.93
Benchmark**	2.61	6.08	28.58	10.12	11.05	9.71
Added Value	(0.46)	(0.81)	1.10	(2.68)	(3.42)	0.22

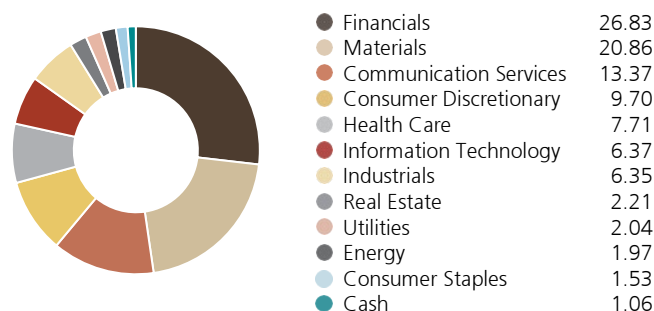
*The UBS Asset Management price/value equities process was adopted on 1 April 1996. **S&P/ASX 300 Accumulation Index. All Ordinaries Accumulation Index prior to June 2000.

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.

Fund information

Inception date	15 July 1992
Fund size	\$312.6m
Management fee	0.90% pa
Minimum initial investment	\$50,000
Typical number of holdings	30 to 70
Distributions	Semi-annually
Buy/sell spread	+/- 0.25%
APIR code	SBC0817AU

Fund positioning (%)



Portfolio review

After fees and expenses, the Portfolio rose by 2.15% during the month, underperforming its benchmark by 46 bps.

The largest positive contributors were Fortescue Metals Group (not held), Rio Tinto (not held) and Carsales.com. Fortescue underperformed as the iron ore price declined 15% to US\$154 per tonne in response to China clamping down on steel output to lessen pollution. The fall overshadowed a strong FY21 result in which FMG delivered record earnings and dividends, with NPAT more than doubling to US\$10.3bn (in line with consensus). Rio Tinto also declined alongside the commodity. Carsales.com outperformed as its FY21 result came in at the top end of guidance issued in May, with revenue and NPAT growing 4% and 11% respectively (y/y). While prolonged lockdowns in NSW and VIC cloud the outlook, CAR still expects 'solid growth' in underlying NAPT for FY22.

The largest negative contributors were BHP Group, Afterpay (not held) and Link Administration. BHP underperformed during the period over uncertainty relating to several major initiatives and the iron ore price falling 15%, which overshadowed its strongest earnings result since FY12. Underlying EBITDA came in at US\$37.4bn, in line with expectations, and the final dividend was a record US\$2.00 per share, with BHP returning US\$15bn to shareholders during FY21. Afterpay received a takeover bid from US digital payments company Square in an all-scrip bid equating to a 30% premium to APT's last traded share price. Link delivered a disappointing FY21 result. While operating NPATA of \$113.2mn was only 2% below consensus, management guided to broadly flat operating EBIT in FY22 – well below consensus for 15% growth due to cost reinvestment.

Market review

Australian equities delivered their best monthly return since November 2020 during reporting season, overcoming uncertainty relating to protracted lockdowns in NSW and VIC and negative earnings revisions across the market.

The S&P/ASX 300 Accumulation Index lifted by 2.6% in August, taking its 12-month return to +28.6%. In comparison, the MSCI Global Index returned 2.7%. However, FY21 reporting season saw more misses than beats despite recording +28% growth y/y, and FY22 forecasts were revised down at -1.2% for the ASX200 and -1.5% for the Small Ords.

Nevertheless, equity valuations rose globally amid lower bond yields, with the US 10-year bond yield declining 21 bps to 1.23% in response to dovish commentary from the US Fed and the Australian 10-year bond yield remaining flat at 1.16%.

Information Technology (+16.2%) was the top performer, supported by Afterpay (APT, +39.2%) as the buy-now pay-later (BNPL) company received a takeover bid from US digital payments company Square in an all-scrip bid equating to a 30% premium to APT's last traded share price. Wisetech Global (WTC, +57.0%) and Xero (XRO, +8.2%) also outperformed following better-than-expected results.

Health Care (+6.6%) was another strong contributor to the benchmark. CSL (CSL, +8.0%) outperformed as a re-opening beneficiary, while ResMed's (RMD, +11.4%) 4Q21 result beat expectations and as a key competitor was forced to issue a product recall.

Conversely, the falling iron ore price (-15%) weighed on mining majors Fortescue Metals Group (FMG, -15.7%), BHP Group (BHP, -14.7%) and Rio Tinto (RIO, -10.7%) even as they delivered better-than-expected dividends and announced major climate change initiatives, with BHP exiting Petroleum in a proposed merger of the division with Woodside (WPL, -9.2%) and Fortescue Metals Group (FMG, -15.7%) announcing 10% of future NPAT would go towards renewable energy projects.

Outlook

The Australia 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 the number of people employed comfortably exceed pre-pandemic levels. Clear highlights were the unemployment rate declining from a peak of 7.5% in July 2020 to just 4.6% in July 2021 and June quarter GDP rising 0.7%, well ahead of expectations. Nevertheless, renewed COVID-related lockdowns in Melbourne and Sydney 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 a 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.

We see significant value in certain sectors but believe others to be overvalued based on our earnings and cash flow expectations. We are most overweight stocks within the Communication Services, Information Technology and Materials sectors, and underweight Real Estate, Consumer Staples and Health Care.

Client Services

Telephone: (03) 9046 4041 Freecall: 1800 572 018 Email: ubs@unitregistry.com.au www.ubs.com/am-australia

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