

# UBS Yarra Microcap Fund

September 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	Pilbara Minerals
Intega Group	Orocobre Limited
Empired	Steadfast Group
Pacific Smiles Group	Iluka Resources
EROAD	ARB Corporation

## Active industry positions

Overweight	Underweight
Software & Services	Materials
Capital Goods	Real Estate
Health Care Equipment & Services	Consumer Services
Commercial & Professional Services	Energy
Technology Hardware & Equipment	Diversified Financials

## Investment Strategy

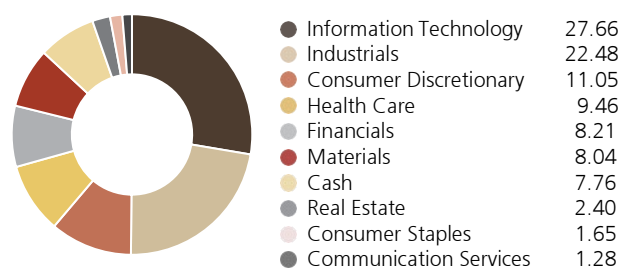
The Portfolio Manager's overarching strategy is to identify those Microcap shares that are believed to be undervalued by the market, based on an assessment of the companies' future cash flows. Normally the Fund will hold between 35–65 stocks in companies with a market capitalisation of generally less 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	\$ 62.1 m
Management fee	1.20% pa
Performance fee*	Yes
Minimum initial investment	\$500,000
Typical number of holdings	35 to 65
Distributions	Semi-annually
Buy/sell spread	+/- 0.70%
APIR code	UBS0057AU

\* 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	(0.48)	5.68	40.28	18.05	14.79	17.23
Benchmark**	(2.14)	3.44	30.41	9.42	10.17	9.80
<b>Added Value</b>	<b>1.66</b>	<b>2.24</b>	<b>9.87</b>	<b>8.63</b>	<b>4.62</b>	<b>7.43</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 decreased by 0.48% during the month, outperforming its benchmark by 166 bps.

The largest contributors were XRF Scientific, Janison Education and PTB Group. XRF provides capital equipment and consumables to laboratories used in the preparation of samples. Strength in the mining industry is leading to strong demand, and the acquisition of 50% of Orbis Mining provides opportunity to cross sell to the existing client base in addition to opening up new market opportunities. Janison Education also continued to perform well post the release of their annual results. The continued shift toward digitization of assessments and the likely increased testing requirements as students return from lockdown provide a supportive backdrop. PTB group, which provides maintenance to turbo prop aircraft engines, has used the pandemic to acquire a foothold in the US market. With an increased market presence and a likely beneficiary of re-opening economies and borders, PTB remains well placed for solid medium-term growth.

The largest negative contributors were Lunnon Metals, Lumos Diagnostics and Flight Centre (not held). Lunnon Metals was subject to profit taking following consistent strong performance since the IPO in June 2021. We remain positive on the longer-term outlook for Nickel and believe the heritage of the assets and lack of recent exploration provide for significant opportunity. Lumos Diagnostics, which is seeking to develop and commercialize point of care diagnostic solutions, was weaker following disappointment around the FDA's decision to deprioritize the emergency use application for their CoviDx Rapid Antigen Test product. FDA approval for FebriDex remains the key near term catalyst, a product which offers significant benefit in the ability to diagnose viral versus bacterial infection. This provides for better treatment outcomes, particularly around the overuse of antibiotics. Flight Centre outperformed as Australian vaccination rates accelerated, pulling forward the timeline for the resumption of domestic and international travel.

## Market Review

Australian equities declined in September as supply disruptions and higher energy prices raised concerns about higher inflation and lower economic growth.

The S&P/ASX Small Ordinaries Accumulation Index declined by 2.1% in the month, taking its 12-month return to +30.9%. In comparison, the broader ASX returned -1.9% and the MSCI Global Index returned -3.6% in local currency terms. Equity valuations reversed some of their recent gains in September as the inflation theme re-emerged and concerns mounted about faster tapering of QE, with the Australian 10-year bond yield rising 33 bps to 1.49%.

Energy (+15.7%) was the top performer during the period, as the emerging gas crisis in the EU/UK and China saw widespread gains across broader commodity complex, with Brent Crude rising 8% to \$US80 per barrel and thermal coal up 25% to \$US218/t. At a stock level, the top performers included Whitehaven Coal (WHC, +27.7%) and Beach Energy (BPT, +42.4%). Elsewhere, travel services stocks rebounded during the period as Australia draws closer to re-opening the economy. Flight Centre (FLT, +30.8%) and Webjet (WEB, +11.4%) were among the top performers.

Conversely, Gold (-11.2%) was among the worst performers during the period, weighed down by ongoing USD strength. The worst performers included Regis Resources (RRL, -17.5%) and De Grey Mining (DEG, -19.6%).

## Outlook

After completing 1H2021 with strong momentum, renewed Covid-related lockdowns in Melbourne and Sydney will see the Australian economy contract in 3Q21, albeit it has been notable how well both business surveys and employment indicators have held up in Q3, suggesting a modest contraction than might have been expected several months ago.

We continue to believe the interruption to economic growth from renewed lockdowns will be an aberration within an improving trend. 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 \$185bn in excess household saving, in concert with strong asset price gains, leaves the consumer uniquely positioned to underpin economic growth in 2021- 2022. Dwelling investment is set to provide solid support for economic growth over the next 6 months as previously approved housing moves through the construction phase, 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% and the Australian economy to expand 4.5% 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%.

Nevertheless, there are some areas that are cause for concern. For over 12 months we have warned about rising US inflation pressures and rising inflation expectations. However, 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 signalling increased willingness to taper its purchases, we expect bond yields will move higher through the remainder of 2021. We expect US 10-year yields to approach 1.80% by the end of 2021, providing some ongoing challenges for risk assets in Q4.

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. We expect the A\$/US\$ to finish the year in the 76-78c range, and remain around that level through 1H22.

## Client Services

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