

UBS Yarra Australian Small Companies Fund

October 2021

Fund description

The Fund is an actively managed fund investing in a portfolio of 30–60 Australian small company equity securities across a range of industry sectors.

Investment strategy

The Portfolio Manager's overarching strategy is to identify those small company shares that are believed to be undervalued by the market. Normally the Fund will hold between 30–60 stocks in companies. Companies are selected for inclusion in the portfolio after a rigorous investment process.

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
IGO	Orocobre Limited
AUB	Steadfast Group
Pinnacle Investment Management	Iluka
Nanosonics Limited	ARB Corporation
Auckland International Airport	Technology One

Active industry positions

Overweight	Underweight
Transportation	Real Estate
Health Care Equipment & Services	Materials
Food Beverage & Tobacco	Retailing
Media & Entertainment	Energy
Insurance	Capital Goods

Investment performance

Fund	1 month %	3 months %	1 year %	3 years % pa	5 years % pa	Since inception* % pa
Total return	0.16	5.99	36.95	19.31	14.97	13.45
Benchmark**	0.92	3.68	31.01	13.51	11.44	6.87
Added Value	(0.76)	2.31	5.94	5.80	3.53	6.58

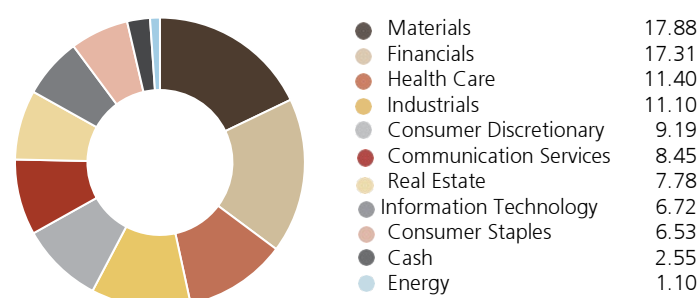
*Inception date: 31 March 2004. **S&P/ASX Small Ordinaries Accumulation Index. Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.

Fund information

Inception date	31 March 2004
Fund size	\$ 144.0 m
Management fee	0.85% pa
Performance fee*	Yes
Minimum initial investment	\$50,000
Typical number of holdings	30 to 60
Distributions	Quarterly
Buy/sell spread	+/- 0.45%
APIR code	UBS0004AU

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

Fund positioning (%)



Top 5 stocks (%)

Pinnacle Investment Management	4.35
AUB	4.02
IGO	3.88
Nanosonics Limited	3.64
Megaport	3.45

Portfolio review

After fees and expenses, the Portfolio rose by 0.16% during the month, underperforming its benchmark by 76 bps.

The largest positive contributors were Imdex, Pinnacle Investment Management and IGO Limited. Imdex delivered a better-than-expected update at its AGM, announcing that revenue grew 41% to \$86.8mn (y/y) in 1Q22 with growth across all regions. Pinnacle also held its AGM during the period, revealing FUM of \$90.2bn in 1Q22 (+0.9% since FY21) that was largely driven by the higher-fee retail channel. IGO Limited outperformed as lithium prices continued to strengthen, with spodumene rising 2% to US\$2,300/t, on top of the 92% rise in the prior month.

The largest negative contributors were Sealink Travel, AUB Group and Select Harvests. Sealink Travel missed out on a \$2.3bn, 9.5-year contract with the Melbourne Metro Bus Franchise, which was instead awarded to Kinetic. AUB Group partially retraced strong outperformance from prior periods despite no material news. Select Harvests partially retraced strong outperformance. Significant rainfall is forecast for California – ending its current drought and bringing more almond supply to market.

Market Review

Australian small caps rose modestly in October, underperforming global equities as Australian bond yields rose sharply in response to higher inflation expectations.

The S&P/ASX Small Ordinaries Accumulation Index rose 0.9% during the month, taking its 12-month return to 26.0%. The local index underperformed global indices – with the MSCI World Index returning 5.5% – as Australian 10-year bond yields lifted 59 bps to 2.08% during the period on expectations the RBA would hike rates earlier amid inflation pressure.

Gold (+13.0%) was the top performer during the period, with the sector seen as a beneficiary of stronger inflation. Within the sector, Silver Lake Resources (SLR, +26.5%) and West African Resources (WAF, +34.0%) were the strongest contributors to the benchmark's return.

Information Technology (+3.3%) also delivered a solid return, with the sector likely supported by lower real yields in the US. The best performing stocks included Life360 (360, +22.4%), Appen (APX, +20.0%) and Nearnmap (NEA, +16.6%).

Conversely, Financials (-1.8%) and Health Care (-3.1%) were the worst performing sectors. The former was weighed down by Pandal (PDL, -19.6%), Zip Co. (Z1p, -7.9%) and Steadfast (SDF, -4.7%), while the latter saw declines from Clinuvell Pharmaceuticals (CUV, -9.9%), Starpharma (SPL, -21.1%) and Nanosonics (NAN, -6.2%).

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. Real-time data suggests Q4 economic growth will rebound solidly, led by the service-based industries.

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. 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 announcing its decision to taper its bond 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, we believe 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.

We are most overweight stocks within the Health Care, Financials and Industrials sectors, and are underweight Consumer Discretionary, Real Estate and Materials.

Client Services

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