

UBS Yarra Microcap Fund

May 2022

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.

Target market

The Target Market Determination (TMD) for the Fund sets out the class of consumers for whom the product, including its key attributes, would likely be consistent with their likely objectives, financial situation and needs. To access to the TMD and other Fund documentation visit our [website](#).

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.

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
Monash IVF Group	Whitehaven Coal
Ridley Corporation	Uniti Group
Mincor Resources NL	NIB Holdings
Alliance Aviation Services	Shopping Centres Australasia Property Group RE
Generation Development Group	Flight Centre Travel Group

Active industry positions

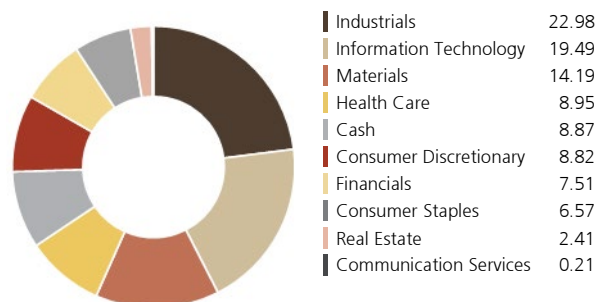
Overweight	Underweight
Capital Goods	Real Estate
Software & Services	Materials
Health Care Equipment & Services	Energy
Food Beverage & Tobacco	Consumer Services
Transportation	Telecommunication Services

Fund information

Inception date	12 August 2014
Fund size	\$ 68.4 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	+/- 0.50%
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 % pa	3 year % pa	5 years % pa	Since inception* % pa
Total return	(7.45)	(6.62)	(1.16)	15.96	14.25	14.22
Benchmark**	(7.01)	(3.58)	(4.56)	5.50	8.49	7.39
Added Value	(0.44)	(3.04)	3.40	10.46	5.76	6.83

*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 7.45% during the month, underperforming its benchmark by 44 bps.

The largest positive contributors were Alliance Aviation, Ridley Corporation and Infomedia. Alliance Aviation rallied on the back of news that an agreement had been reached with Qantas to fully acquire the company in a deal worth \$4.75 per share, subject to ACCC approval. Ridley Corporation also traded higher after providing further detail on their growth plans, which are anticipated to deliver total shareholder returns of 15% p.a. over the next two financial years. Infomedia received competing takeover proposals during the period. Private equity firm TA Associates lobbied the first bid at \$1.70 per share, a 33% premium to its last traded price, before Batter Ventures subsequently proposed an improved offer of \$1.75 per share.

The largest negative contributors were Atomos, Pacific Smiles and Calidus Resources. Atomos traded lower after reducing revenue guidance from \$95m to between \$80-\$90m and its EBITDA margin from 12-15% to 6-8%. Pacific Smiles was sold off on the back of an April trading update confirming patient fees declined 8.2% YoY, highlighting the business continues to be disrupted by COVID-19 resulting in poor patient attendance and practitioner availability. Calidus Resources traded lower following a weakened underlying gold price despite reaching the milestone of its first Gold pour.

Market review

Australian small caps declined during May as Australia's first interest rate hike since 2010 pressured valuations, with only the Energy sector recording a positive return.

The S&P/ASX Small Ordinaries Accumulation Index returned -7.0% for the month, taking its 12-month return to -4.6%. In comparison, the broader ASX300 declined 2.8% for the month while global indices were flat (MSCI World Index -0.2%). Following the decline, the Small Ords trades at a one-year forward P/E of 13.8 times, 17% below its 5-year average.

Within Energy (+2.7%), coal producers continued to rise in value amid the global energy crisis. While hard coking coal retreated 15% during the month to US\$442/t, thermal coal rose another 31% to US\$427/t. Whitehaven Coal (WHC) – now the largest constituent in the index – climbed +7.3% and New Hope Corporation (NHC) lifted +5.7%.

Conversely, the worst performing sectors included Consumer Discretionary (-10.9%) and Metals & Mining (-8.5%). In the former, travel services companies Corporate Travel Management (CTD, -15.5%) and Flight Centre (FLT, -9.3%) underperformed as updates suggested ongoing lower margins for international travel. In the latter, emerging lithium project developers including Sayona Mining (SYA, -31.3%) and AVZ Minerals (AVZ, -21.2%) declined sharply.

Elsewhere, Real Estate (-8.0%) also experienced widespread declines given its negative correlation to higher rates, led by Centuria Capital Group (CNI, -20.7%), Centuria Industrial REIT (CIP, -14.0%) and Home Consortium (HMC, -17.2%).

Outlook

Geopolitical events and surging commodity prices have taken centre stage in 2022, shaking risk sentiment and challenging consensus' optimistic forecast for global growth. From our perspective, although for the past six months our forecasts for global growth in 2022 have been below consensus, we believe a series of downgrades will soon be evident for global earnings growth in most major markets. Surging commodity prices and ongoing supply shortages have resulted in further upside to the inflation outlook and risks forcing the hand of central banks in coming months to try to contain rising inflation expectations. The reality for 2022 is likely a world of higher inflation, slower growth and higher financing costs awaits.

Australia does have some key natural advantages in such a climate. One of the most notable is that Australia's export dominance of iron ore, coal, LNG, gold, wheat and base metals contribute close to 80% of Australia's exports and each of these commodities have seen strong price rises in 1H 2022 which will likely translate into a large positive national income boost even if spot prices retreat in coming weeks. Indeed, Australia presents as a safe haven market which is far from the conflict in Europe, an exporter of in demand raw materials and given its own undershooting of its inflation target since 2015 it has ample room to adjust policy settings at a gradual pace.

Australia also has the benefit of recovering underlying household income growth, \$230bn in 'excess saving', strong corporate profit growth, robust capex expectations in concert and improving government finances which suggests Australian economic growth in 2022 will remain more robust than its developed economy peer group. In CY2022 we expect the Australian economy to expand at an above 'potential' rate of 3%.

While this is slower than the 4% pace recorded in 2021 it is still sufficient to see further employment growth gains and we expect the unemployment rate will soon fall below 4% and below the RBA's estimate of non-accelerating inflation rate of unemployment (NAIRU) and further wage pressure will become evident into mid-2022.

While the RBA has been later than most other developed nations in tightening policy, tighter financial conditions in 2022 are likely to come via both significantly higher cash rates and a stronger currency. The A\$/US\$ has in recent months been buffeted by concerns of a peak in global industrial growth indicators and slowing China economic momentum. Nevertheless, Australia's external accounts are in their best position since the early 1970s and surging commodity prices in early 2022 is providing an incentive for the A\$/US\$ to commence an appreciation cycle, together with the attractive carry on offer. We expect the A\$ will finish 2022 at around 76 cents, albeit the risk to this forecast is on the upside.

Client Services

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

Any financial product advice in this document is general advice only and has been prepared without taking into account your personal objectives, financial situation or particular needs. Therefore, before acting on any advice, you should consider the appropriateness of the advice in light of your own or your client's objectives, financial situation or needs. Investors should consider the Product Disclosure Statement (PDS) and seek professional financial and taxation advice before deciding whether the product is appropriate for them and whether to acquire, or to continue to hold the investment. Your investment in the Fund does not represent deposits or other liabilities of UBS AG or any member company of the UBS Group including UBS Asset Management (Australia) Ltd (ABN 31 003 146 290) (AFS Licence No. 222605), the issuer and responsible entity of the Fund. Your investment is subject to investment risk, including possible delays in repayment and loss of income and capital invested. The repayment of capital or income is not guaranteed by any company in the UBS Group. Offers of interests in the Fund including the details of the management fee received by the responsible entity are contained in the PDS dated 29 September 2021. The responsible entity has also issued a target market determination (TMD) that describes the class of consumers that comprises the target market for the Fund and matters relevant to its distribution and review. A copy of the PDS (including the PDS additional information booklet) and TMD are available on our website at <https://www.ubs.com/au/en/asset-management.html> or by calling (03) 9046 4041 or 1800 572 018.

The PDS and application form is only available to persons receiving it (electronically or otherwise) while physically in Australia, unless expressly authorised by us in writing. The offer does not constitute an offer or invitation in any place in which, or to any person to whom, it would be unlawful to make such an offer or invitation. The Fund (or the PDS) has not been registered under the laws of any jurisdiction outside Australia. The Fund may not be offered or sold in the United States of America or to 'U.S. Persons' (as defined in 'Regulation S' of the Securities Act of 1933, as amended).

This document may not be reproduced or copies circulated without prior written authority from UBS Asset Management (Australia) Ltd.

Yarra Funds Management Limited (ABN 63 005 885 567, AFSL 230 251) is the portfolio manager of the Fund. The information set out has been prepared in good faith and while Yarra Funds Management Limited and its related bodies corporate (together, the "Yarra Capital Management Group") reasonably believe the investment information and opinions to be current, accurate, or reasonably held at the time of publication, to the maximum extent permitted by law, the Yarra Capital Management Group: (a) makes no warranty as to the content's accuracy or reliability; and (b) accepts no liability for any direct or indirect loss or damage arising from any errors, omissions, or information that is not up to date.

Yarra Funds Management Limited manages the Fund and will receive a fee that is paid from the fee received by the responsible entity and described in the PDS. To the extent that any content set out in this presentation discusses market activity, macroeconomic views, industry or sector trends, such statements should be construed as general advice only. Any references to specific securities are not intended to be a recommendation to buy, sell, or hold such securities. Holdings may change by the time you receive this report. Future portfolio holdings may not be profitable. Past performance is not an indication of, and does not guarantee, future performance.

References to indices, benchmarks or other measures of relative market performance over a specified period of time are provided for your information only and do not imply that the portfolio will achieve similar results. The index composition may not reflect the manner in which a portfolio is constructed. Portfolio characteristics take into account risk and return features which will distinguish them from those of the benchmark.