

UBS Yarra Microcap Fund

July 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	NIB Holdings
Ridley Corporation	Shopping Centres Australasia Property Group RE
GR Engineering Services	Technology One
Lycopodium Limited	Chorus
Generation Development Group	Beach Energy

Active industry positions

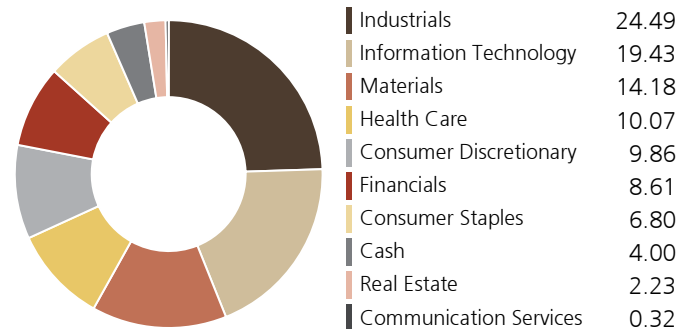
Overweight	Underweight
Capital Goods	Real Estate
Software & Services	Materials
Health Care Equipment & Services	Energy
Food Beverage & Tobacco	Consumer Services
Transportation	Telecommunication Services

Fund information

Inception date	12 August 2014
Fund size	\$ 61.4 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	9.22	(9.36)	(8.05)	12.51	12.98	13.61
Benchmark**	11.43	(9.94)	(10.93)	2.54	7.30	6.80
Added Value	(2.21)	0.58	2.88	9.97	5.68	6.81

*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 9.22% during the month, underperforming its benchmark by 221 bps.

The largest positive contributors were Praemium, Jayride and Monash IVF. Praemium bounced off recent lows following the release of their quarterly update highlighting net inflows for the financial year of \$2.9bn up 92% on the prior corresponding period. Jayride reached the key milestone of a positive free cash flow quarter with a record 136,000 trips booked, well above pre-pandemic levels. Monash IVF announced the acquisition of ART Associates Queensland providing a strategic expansion to the existing Brisbane business. The acquisition included 6 fertility specialists who are anticipated to transition patients over to Monash IVF, increasing group earnings per share of between 5-10%.

The largest negative contributors were Ridley Corporation, Alliance Aviation and RPM Global. Ridley Corporation fell on no company specific news however the outbreak of foot and mouth disease in neighbouring Indonesia was a cause for concern. Alliance Aviation traded lower as the ACCC ruling on the proposed takeover from Qantas at \$4.75/share neared. RPM Global ended the month lower despite providing a positive update on software subscriptions which increased by \$5.6m to \$55.9m in the final four days before the end of financial year.

Market review

Australian equities rallied sharply during July, following the 9% decline in June, as market expectations increased that interest rates have peaked.

The S&P/ASX Small Ordinaries Accumulation Index returned +10.7% for the month, taking its 12-month return to -10.9%. In comparison, the broader ASX300 gained 5.9% for the month and global indices were positive.

Within Healthcare (+14.3%), previously constrained growth rates had been interrupted by COVID and access to hospitals, however, access is now resuming and higher risk, pre-profit companies such as Telix Pharmaceuticals (TLX, +63.1%) and Mesoblast (MSB, +53.3%) found support.

Within Financials (+18.3%), Zip Co (ZIP, +158%), Pinnacle Investment Management (PNI, +42.4%) and Australian Ethical Investment (AEF, +40.1%) outperformed.

Conversely, the worst performing sector was Consumer Staples (-2.7%) which was dragged lower by Australian Agricultural Company (AAC, -14.3%), Elders (ELD, -10.4%) and Costa (CGC, -10.1%), companies which had previously been safe haven stocks and have negative correlations with inflation.

Outlook

Financial markets have now embraced the risk of recession in the US and Europe over the past quarter and the gap between our more pessimistic forecasts for the global economy and the consensus has narrowed. Indeed, with the Fed signalling that financial conditions are close to neutral, we are edging closer to the point where the pace of monetary tightening will slow, providing some scope for risk markets to recover some lost ground.

Indeed, the period of excess inflation is starting to recede with prior surges in commodity prices retreating, an easing in supply constraints, and signs of slowing demand likely to compress elevated sales margins. As central banks continue to await firmer signs that inflation expectations have stabilised and for labour demand to ease, financial markets are faced with the positive news of less restrictive monetary policy and the negative news of likely weaker company earnings.

In a world of heightened concerns of recession in major developed economies, subdued economic activity in China and ongoing conflict between Russia and the Ukraine which has contributed to commodity shortages, high inflation and rising interest rates, the Australian economy presents as a relative safe haven.

Australia's economic data has remained robust in 1H2022, and although we do expect economic activity to slow in FY23 we do not expect a recession in Australia due to three key reasons:

1. Australia has been a net beneficiary of global commodity shortages. This surge in commodity prices saw Australia's export prices in A\$ terms move to their highest levels since the 1880s in 1H2022. The consequence has been strong national income growth, profits growth and an improving underlying fiscal position.
2. The household sector continues to hold a significant buffer of over \$150bn of excess savings (approximately 7% of GDP) relative to pre-COVID levels. Although we expect the impact of higher interest rates and higher living expenses to curtail consumer spending, we do expect the combination of rising wage growth and a run down in the level of savings to continue to support consumption spending.
3. Low levels of spare productive capacity, strong profit and low corporate debt have contributed to robust capital investment intentions.

Over the medium term we believe a recovery in net immigration levels into Australia and Australia's exposure to the key commodities crucial to the global energy transition – including copper, lithium and iron ore – will provide a solid underpin for future economic growth.

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. While we expect that the RBA Cash Rate will finish the year at less than 2.5%, below market expectations of 3.0%, the A\$ risk continues to skew to the upside. Australia's external accounts are in their best position since the early 1970s, providing an incentive for the A\$/US\$ to commence an appreciation cycle, together with the attractive carry on offer, improving China economic data and the prospect the US\$ uptrend will peak as the Fed pivots from its aggressive hiking strategy. We expect the A\$ will finish 2022 at around 76 cents.

Client Services

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