

Ironbark Karara Australian Small Companies Fund

BENCHMARK

 S&P/ASX Small Ordinaries
 Accumulation Index

OBJECTIVE

To outperform the benchmark (before fees) over rolling 4-year periods.

APIR

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ARSN

114 291 486

INCEPTION DATE

30 June 2005

MANAGER APPOINTED

1 May 2010

MANAGEMENT FEE

1.1275% p.a.

FUND SIZE

\$448.2m

BUY / SELL SPREAD

+0.20% / -0.20%

EXIT PRICE

\$3.5676

Net performance (%)

	1 month	3 months	1 year	3 years p.a.	5 years p.a.	10 years p.a.	Since inception p.a. ¹
Fund	1.09	-1.56	37.79	5.98	7.86	7.27	11.99
Benchmark	0.79	2.09	52.15	8.33	10.69	4.11	5.12
Active	0.30	-3.65	-14.36	-2.35	-2.83	3.16	6.87

Top 5 monthly contributors and detractors

Contributing stocks	Active position	Detracting stocks	Active position
SeaLink Travel Group	Overweight	Cooper Energy	Overweight
Uniti Group	Overweight	IGO	Overweight
Ramelius Resources	Overweight	Premier Investments	Underweight
Vocus Group	Overweight	Harvey Norman	Underweight
Elders	Overweight	Ama Group	Overweight

Top 5 quarterly contributors and detractors

Contributing stocks	Active position	Detracting stocks	Active position
Uniti Group	Overweight	Zip Co	Underweight
SeaLink Travel Group	Overweight	Nuix	Overweight
Vocus Group	Overweight	Cooper Energy	Overweight
Elders	Overweight	Ama Group	Overweight
Nanosonics	Underweight	Meridian Energy	Overweight

Top 5 holdings (In alphabetical order)

Stocks	Sector
Elders	Consumer Staples
Mineral Resources	Metals & Mining
SeaLink Travel	Consumer Discretionary
Uniti Group	Communication Services
Vocus Group	Communication Services

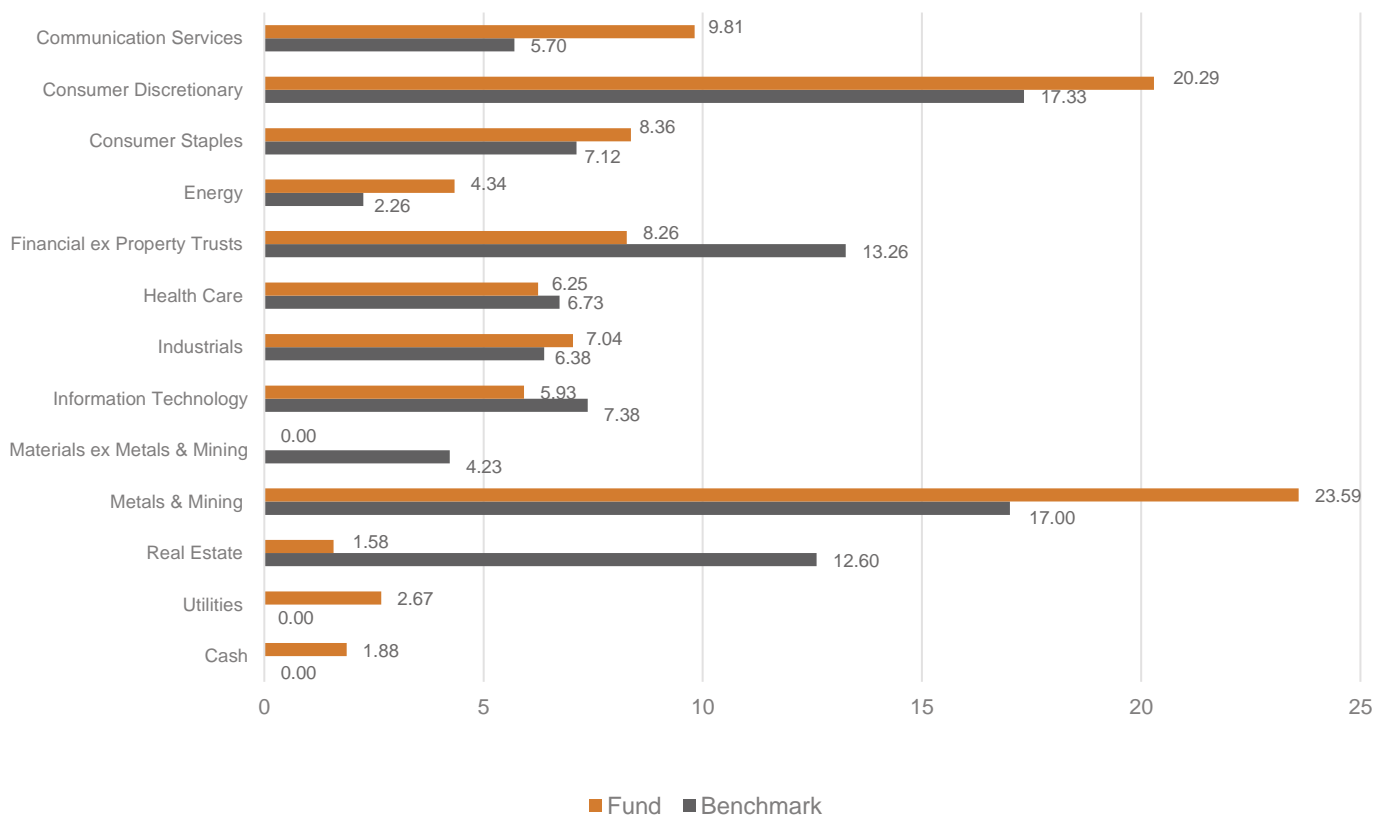
Past performance is not indicative of future performance. Net performance figures are calculated using exit prices, net of fees and reflect the annual reinvestment of distribution. Returns are rounded to two decimal places. Slight variations to actual calculations may occur.

¹This figure represents the annualised performance of the Fund since inception.

CONTACT DETAILS

T.1800 034 402 | E. Client.Services@ironbarkam.com | W. www.ironbarkam.com

Sector asset allocation (%)



Market review

In Australia, the broad-based S&P/ ASX 300 Index rose 4.15% while the Small Ordinaries Index gained 2.09%.

The Reserve Bank flagged the extension of record low interest rates until at least 2024 and doubled the size of its daily quantitative easing bond purchasing program from \$2 billion to \$4 billion. Reserve Bank of Australia's Governor, Philip Lowe said the economic recovery was faster than expected and that gross domestic product was now expected to return to its pre-pandemic level by the middle of this year. The outlook, however, would depend on the success of the vaccine rollout that meant keeping record low rates pinned for at least another three years.

Australia's unemployment rate fell to 5.8% (from 6.3% in January) following strong jobs growth of 88,700. The sharp drop in net overseas migration due to international border closures raises the likelihood that wages growth lifts as the labour market tightens.

Amongst commodities, Saudi Arabia surprised the oil market with a large reduction in output for February and March, sending oil prices higher (West Texas Intermediate up 22%). Iron ore finished higher despite some volatility during the quarter. Copper up 17%. Precious metals remained soft as US rates continue to rebase higher, with gold falling 9%.

Performance review

The Ironbark Karara Australian Small Companies Fund fell -1.56% (net) during the March quarter. This constituted 3.65% of underperformance when compared with the benchmark S&P/ASX Small Ordinaries Accumulation Index return of 2.09% for the three months.

The strongest contributors to Fund performance at a sector level were overweight positions in Communication Services and Consumer staples. An underweight position in Financials and overweight position in Information Technology detracted from relative performance.

At a stock level, positive contributors to quarterly performance included overweight positions in Uniti Group, SeaLink Travel, Vocus Group and Elders. Not holding Nanosonics also contributed to relative performance.

Performance review (continued)

Uniti shares added 35% on the back of a strong first half financial year result that reflected rapid growth over the past twelve months from the highly cash-generative businesses acquired and consolidated. Reported earnings before interest tax depreciation and amortisation (EBITDA) of \$29 million was \$22 million higher than the prior period, underpinned by the Wholesale & Infrastructure (W&I) division. W&I reported annualised EBITDA of \$100 million as at December and is poised for further growth given a contracted pipeline of 202,000 premises which, if converted to active premises as expected within the next five years, will add approximately \$79 million of EBITDA based on established activation rates.

SeaLink shares rose 37% following a strong first half financial year result, 30% ahead of expectations. Formal guidance for the full year was not provided however trading remains robust and the key short-term drivers include previously announced contract wins and extensions, further Sydney bus efficiencies and a 6-month contribution from the Brisbane ferry contract which commenced in November 2020. SeaLink's medium-term growth strategy remains focused on government bus tenders in Sydney and Melbourne and possible expansion into new markets.

Shares in Vocus rose 35% after announcing it had entered a binding Scheme Implementation Deed with MIRA/Aware Super for it to acquire Vocus for \$5.50 cash. This followed the announcement in February that the Company had received an indicative and non-binding proposal. Subject to no other competing bid, the board has recommended shareholders vote in favour which should see it completed sometime in July 2021.

Elders gained 26% on the back of upgrades to consensus earnings estimates due to very strong seasonal conditions on the east coast of Australia. The rainfall in March across key cropping regions of NSW has given farmers confidence to plant for the 2021 winter crop. Livestock prices have also strengthened, particularly cattle, as farmers look to rebuild herds after the significant drought years of 2018/2019. These dynamics were also evident in strong trading updates from several industry participants including Nutrien, which reported a "stellar performance in Australia" in the December quarter and Nufarm, which reported revenue in APAC up 46% year on year for the 4 months to 31 January.

The largest detractors from quarterly performance included overweight positions in Nuix, Cooper Energy, AMA, and Meridian Energy. An underweight position in Zip Co also detracted from relative performance.

Nuix fell 37% after the first half financial year result missed expectations, increasing the risk profile around financial year earnings delivery, although guidance was maintained. The company experienced delays in signing up US government customers but expressed confidence in revenue visibility, which was strong in the second half.

Cooper Energy fell 31% as the Orbest Gas Plant (operated by APA Group) has yet to consistently meet its near-term targets for gas production of 45 terajoule/day. In a subsequent recent update in early April, Cooper confirmed it is close to reaching the initial target of 45 terajoule/day on a consistent basis and further capital works will be undertaken to increase production to around 55 terajoule/day, still below the targeted name plate capacity of 68 terajoule/day.

AMA Group lost 31% after the company reported a mixed first half financial year result with Jobkeeper benefits, business divestments and a paint supplier termination fee making like for like comparisons difficult. Pleasingly, the balance sheet de-levered in line with expectations however, the market punished the stock after the new CEO was unwilling to provide an update on the timing of a recovery in margins and current trading conditions for the second half financial year.

Meridian Energy fell 28% in a reversal of the move seen in the December quarter as a result of exchange traded fund (ETF) flows and rebalances. In this instance, the de-weighting of Meridian within the Ishares Global Clean Energy ETF represents an overhang in the stock with the shares sold off accordingly. Rising bond yields also represented a share price headwind during the quarter.

Market outlook

The vaccine rollout foreshadows the resolution of the health crisis and this should enable the reopening of most of the developed world by the end of 2021. Despite inevitable logistical hiccups in vaccination, the unwinding of the growth sapping and distortive lockdown measures means the global economic recovery should gain pace in 2021, driven by private consumption and supported by continuing and aggressive fiscal and monetary stimulus.

A lasting impact of COVID 19 has been a reorientation of public policy. Fiscal and monetary policy are now pulling in the same direction. Central banks are targeting employment and promising not to move until inflation is sustained at higher levels. Meanwhile governments (nor voters) no longer seem fussed by government budget constraints and growing debt burdens. The investment manager expect policy support will continue to underwrite economic activity in the near term, but with implications for longer term growth and inflation.

Upward price pressure in intermediate and finished products is now broadly observable. This is being driven by rebounding demand, disrupted supply chains and precautionary inventory building. Elements of this are likely transitory, however implied inflationary break evens have risen significantly recent months and real interest rates have moved higher.

As inflationary expectations have moved through 2%, the debate about the prospects for longer term inflation is heating up. This is awkward for the positioning of benchmarks and strategies which, over the past decade, have progressively re-orientated towards long duration assets and which will fare badly if the consensus view of the risks around inflation changes.

Market outlook (continued)

In the absence of further Central Bank intervention (e.g., quantitative easing of some other variant of yield curve control), the investment manager expects interest rates to continue to adjust higher as the cyclical upturn broadens, the output gap narrows, and the level of incremental liquidity injected is pared back. This should continue to support the reflation trade with shorter duration assets (value) should do better relative to longer ones (growth), supported by a rebound in corporate profits, especially in industries where demand has been suppressed.

For now, while real interest rates remain negative, and long-term rates remain far below average government borrowing costs and, most importantly, central banks very wary of tightening too early, this is unlikely to seriously concern investors as it would be unusual for markets to fall due to an overdose of liquidity.

The surge of earnings upgrades has helped absolute valuations which had been at historically high levels. However, for most sectors they remain at levels that have been seen very rarely, and from which extended bear markets have followed. Further earnings over-delivery will need to be sustained and this will become hard as expectations and input costs rise.

The emergence of some corporate activity among the value sector since late last year, the investment manager thinks, is a broader manifestation of investor impatience with lower growth companies in a difficult operating environment. The gap between earnings yields and the cost of money is attractive for corporates, activist investors, and financial sponsors.

Australia is better positioned than most developed countries. Unemployment has not reached the peaks expected, stimulus is fuelling a recovery and house prices are recovering strongly. Terms of trade have recovered sharply boosting national income. The outlook is underpinned by still relatively low levels of public debt and inbound migration, which will likely return in due course as the fundamental attraction to live here or travel here has likely only been strengthened because of its handling of the pandemic. The investment manager expects strong consumer sentiment and wealth effects will support normalisation in the savings rate this year, which will benefit spending.

Despite the recovery and some obvious risks, the investment manager still sees some opportunities to build positions in quality companies at attractive prices. As seen in 2009, and have started to see again, substantial returns are on offer when companies can transition from fears of declining growth or short-term earnings risk, back to a profile that the market is prepared to construe as sustainable steady growth. Further, the impact of COVID 19 and associated policy responses has accelerated structural change in several industries and this in turn, has led to a number of new and exciting companies seeking to IPO, further broadening our investment opportunity universe.

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