

# Ironbark Karara Australian Small Companies Fund

**BENCHMARK**

S&amp;P/ASX Small Ordinaries Accumulation Index

**OBJECTIVE**

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

**APIR**

PAT0002AU

**ARSN**

114 291 486

**INCEPTION DATE**

30 June 2005

**MANAGER APPOINTED**

1 May 2010

**MANAGEMENT FEE**

1.1275% p.a.

**FUND SIZE**

 \$442.2m<sup>1</sup>
**BUY / SELL SPREAD**

+0.20% / -0.20%

**EXIT PRICE**

\$3.5519

<sup>1</sup>FUM size is reported post-distribution.

**Net performance (%)**

	1 month	3 months	1 year	3 years p.a.	5 years p.a.	10 years p.a.	Since inception p.a. <sup>2</sup>
<b>Fund</b>	<b>3.26</b>	<b>9.22</b>	<b>22.47</b>	<b>7.03</b>	<b>7.71</b>	<b>8.87</b>	<b>12.41</b>
Benchmark	3.08	8.50	33.23	8.60	11.24	5.99	5.58
Active	0.18	0.72	-10.76	-1.57	-3.53	2.88	6.83

**Top 5 monthly contributors and detractors**

Contributing stocks	Active position	Detracting stocks	Active position
Mineral Resources	Overweight	Silver Lake Resources	Overweight
Jumbo Interactive	Overweight	Ramelius Resources	Overweight
Uniti Group	Overweight	Pro Medicus	Underweight
IRESS	Overweight	De Grey Mining	Overweight
Johns Lyng Group	Overweight	Iluka Resources	Underweight

**Top 5 quarterly contributors and detractors**

Contributing stocks	Active position	Detracting stocks	Active position
Mineral Resources	Overweight	EML Payments	Overweight
Uniti Group	Overweight	Carbon Revolution	Overweight
Jumbo Interactive	Overweight	Chalice Mining	Underweight
ARB Corporation	Overweight	Costa Group Holdings	Overweight
IRESS	Overweight	Elders	Overweight

**Top 5 holdings (In alphabetical order)**

Stocks	Sector
ARB Corporation	Consumer Discretionary
Ingenia Communities Group	Real Estate
Mineral Resources	Metals & Mining
SeaLink Travel Group	Consumer Discretionary
Uniti Group	Communication Services

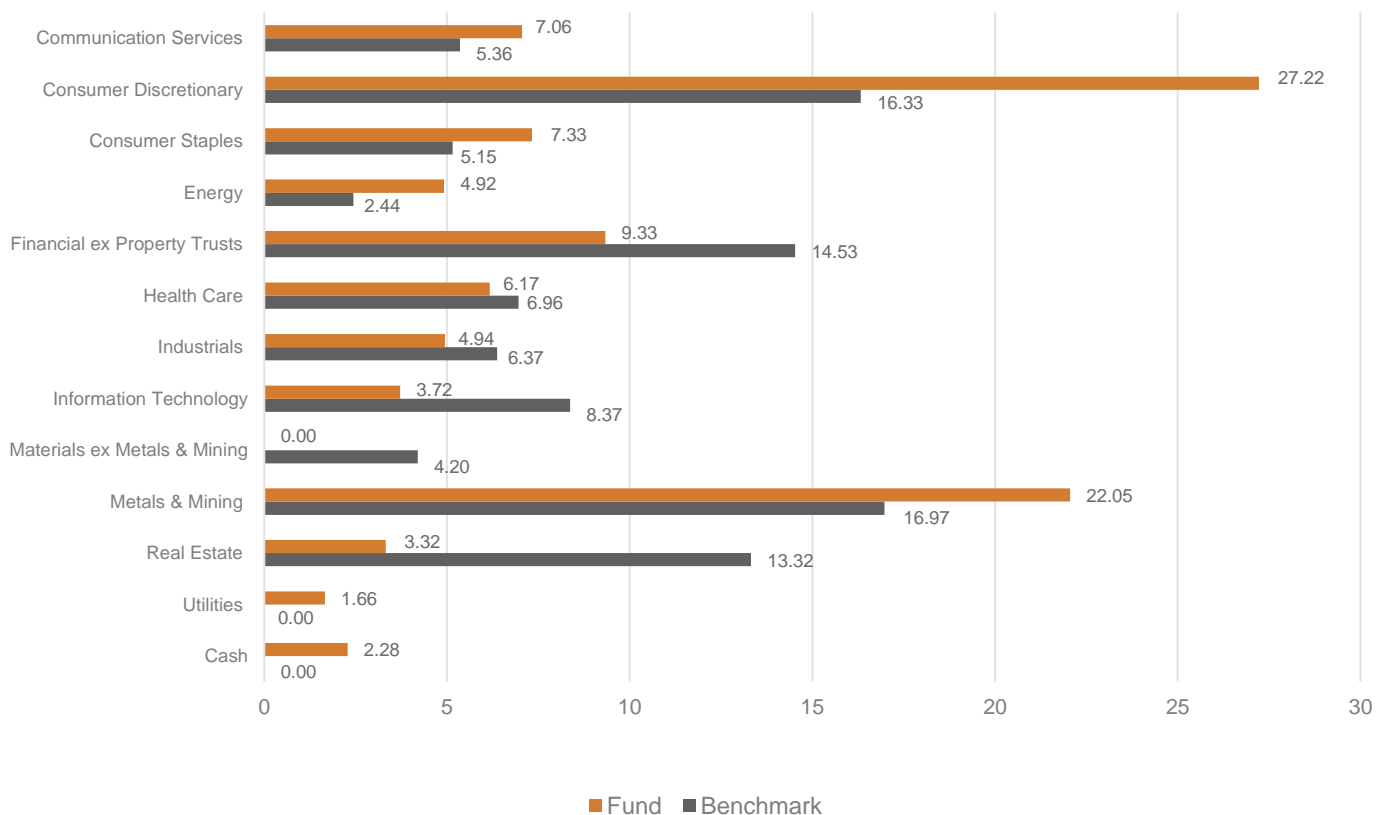
Past performance is not indicative of future performance. Net performance figures are calculated using exit prices, net of fees and reflect the annual reinvestment of distribution. Returns are rounded to two decimal places. Slight variations to actual calculations may occur.

<sup>2</sup>This figure represents the annualised performance of the Fund since inception.

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## Sector asset allocation (%)



## Market review

Australia's economy expanded faster than expected in the quarter as unprecedented fiscal and monetary policy stimulus continued to fuel a strong rebound from the pandemic. GDP grew 1.8% in seasonally adjusted terms quarter-on-quarter, exceeding the 1.5% rise expected by economists. The Australian economy is now 0.4% larger than in December 2019 before the pandemic and associated lockdowns caused the largest economic contraction in 90 years.

Unemployment unexpectedly plunged to pre-COVID-19 levels of 5.1% in May after the number of employed Australians surged by 110,000, triple the expected figure. Unemployment is now running six months ahead of the Reserve Bank's forecast that it would end 2021 at 5%, raising the spectre of the Reserve Bank lifting rates earlier than forecasted should the rapidly tightening jobs market lead to a stronger than anticipated pick-up in worker pay.

Although the economy continues to defy expectations, the Reserve Bank continues to wait to be confident this will show up in wages and inflation before dialling back its monetary stimulus.

Commodity prices were sharply higher given the predominant reflation expectations in place for most of the quarter before a late dip. Iron ore, which rose 30%, was the standout amidst a seasonal lull in Brazilian production and strong demand from China. Oil rose (WTI up 24%, Brent up 20%) on signs of demand recovery in the US and Europe, before a breakdown in OPEC talks triggered fears of a repeat of last year's price war. Copper ended the month up 6%, nickel up 13%, aluminium up 14%, zinc up 7%, while the gold price rose 5% (2% in US dollar terms).

## Performance review

The Ironbark Karara Australian Small Companies Fund rose 9.22% (net) during the June quarter. This constituted a 0.72% outperformance when compared with the S&P/ASX Small Ordinaries Accumulation Index return of 8.50% for the three months.

## Performance review (continued)

The strongest contributors to Fund performance at a sector level were overweight positions in communication services, consumer discretionary and metals & mining. An underweight position in information technology detracted from relative performance.

At a stock level, positive contributors to quarterly performance included overweight positions in Mineral Resources, Uniti Group, Jumbo Interactive, ARB and IRESS.

Mineral Resources shares gained 41% over the quarter, in tandem with a 30% rise in the iron ore price and a 35% gain in the lithium price. The company hosted a three-day site visit of its WA mining operations during the period that coincided with the iron ore price hitting ten-year highs. Mineral Resources outlined ambitious growth plans that included doubling the mining services business, lifting iron ore volumes from 20 to 90 metric tonne per annum, and near doubling its lithium volumes, at the same time converting all spodumene to hydroxide.

Uniti shares added 44% as part of a sustained re-rating following strong financial year 2021 year-to-date results and investor repositioning out of takeover target Vocus Group, given Uniti's similar status as a highly cash-generative telecommunications business with infrastructure-like fibre assets.

Jumbo Interactive shares gained 40% following a spate of higher jackpots in the first half of the year that implies re-seller turnover and revenue growing around 30% following two soft jackpot halves. The investment manager sees current demand as part temporary with prize reserves being released after reaching upper limits, and part structural, as strong like-for-like sales imply a degree of sustained change. Even with post COVID-19 retail channels open, the investment manager continues to expect digital penetration to rise as customers become more accustomed to purchasing lottery tickets online.

ARB shares rose 26% following strong new vehicle sale data, which along with supply constraints, suggest current favourable trading conditions will continue into 2022 financial year. The recent collaboration with Ford in the US provides further benefits to brand awareness in export markets.

IRESS shares added 41% after the company provided an update on the Board's plans to accelerate earnings-per-share growth, provide capital management and divest its mortgage sales & origination business. The timing followed prior day reports that an unnamed buyer was seeking 10% of the company at a material premium to the prevailing share price.

Notable detractors from quarterly performance included overweight positions in EML Payments, Carbon Revolution and Costa Group.

EML fell 41% after the Central Bank of Ireland queried the company's anti-money laundering and know-your-client practises. The concerns may be promptly addressed and resolved with perhaps higher associated compliance costs, however in the worst-case scenario, the company's licence could be revoked which would not only materially impact current earnings, but also the future growth potential of the business.

Carbon Revolution shares declined 48% after the company raised \$95 million to fund the first stage of its mega-line investment. The first stage represents an additional 75,000 wheels of annual production capacity, the incremental return on which when fully utilised remains highly attractive. The additional wheels are for two existing original equipment manufacturer (OEM) customers and introduces four new models. Despite the news about new customers and the additional capacity, the company also downgraded their 2021 financial year guidance from the previous guidance of strong sales growth over the 2020 financial year to now be 1,800 wheels lower.

Costa Group shares declined 27% after a trading update at the company's annual meeting revealed strong international market conditions were being offset by mixed domestic conditions and outlook. The deterioration in domestic conditions was materially below the investment manager's expectations which raises the question as to the extent of elevated consumption demand the group benefited from during peak pandemic months of 2020.

## Market outlook

Following the most recent US Federal Reserve FOMC meeting and Federal Reserve officials' public comments evincing a growing recognition of more-than-a transitory risk of inflation, the near-term outlook for markets is likely to be driven by still-evolving perceptions of potential Federal Reserve monetary tightening. That may be a slow-down in bond purchases ("tapering") or possible increases in short-term interest rates, including increases that may not even occur until late calendar 2022. In any case, the "lift off" vernacular has re-appeared.

The sensitivity of equity markets to daily "Fedspeak" is a salient reminder of the significant impact ultra-loose monetary policy has had on global markets for more than a decade. For now, global bond markets appear to be comfortable with the "transitory" narrative of recent elevated inflation measures and will be key to watch going forward.

## Market outlook (continued)

Major global economies continue to re-open at an encouraging rate despite some delays in the COVID-19 vaccine roll-out and the emergence of the more virulent Delta strain. This is contributing to rising inflationary pressures, particularly when viewed against some permanent loss of supply side capacity through 2020, re-onshoring of some industries, and tighter international freight conditions. Record government stimulus and transfer payments have also created labour market distortions and may indirectly contribute to inflationary pressures if they are sustained. Domestically, a strong re-bounce in employment, restricted Federal borders, and reduced labour force mobility due to intermittent State border closures are contributing to rising wage pressures which have not yet proved inflationary but may ultimately do so. This may test the Reserve Bank of Australia's resolve to keep interest rates low for an extended period.

For now, real interest rates remain negative, long term rates remain far below average government borrowing costs and importantly, central banks remain wary of tightening too early. Despite the recent incrementally more hawkish under-tones from a number of central banks around the world, growth in current fiscal deficits and seemingly ever-expanding overall government debt levels will likely constrain any meaningful increase in nominal rates for some time.

With market multiples elevated headed into August reporting season, earnings upside surprise will need to be delivered which will become harder in the context of rising input costs. COVID 19 and related government policy distortions including the impact of domestic lockdowns are likely to affect a number of industries and sectors in different ways, with some permanent or structural effects being accelerated, while others will prove to have been more fleeting. As such, a deep understanding of each individual company's operating environment will be key to identifying the out-performers.

The investment manager is encouraged by the outlook for several of the Fund's holdings heading into reporting season, a few of which have embedded growth profiles which the investment manager believes may extend for a number of years and are yet to be fully recognised by the market. The investment manager expects the recent pick-up in corporate activity in the small companies space to continue, with the gap between earnings yields and the cost of money remaining attractive for corporates, activist investors and financial sponsors.

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