Yarra Australian Real Assets Securities Fund

Gross returns as at 30 April 2021

	From 17 December 2015	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception^ % p.a.
Yarra Australian Real Assets Securities Fund	8.84	2.68	5.70	15.68	8.50	7.17	9.29	8.32
S&P/ASX Custom Infrastructure, Utilities and A-REITs Index*	7.25	2.65	5.35	15.13	5.89	5.81	NA	NA
Excess Return†	1.59	0.03	0.35	0.56	2.60	1.36	NA	NA

Past performance is not a reliable indicator of future performance. Taxes payable by investors have not been taken into account. The figures shown have been provided for illustrative purposes – they are unaudited and subject to change. The total returns shown are gross of all fees, meaning they do not reflect the deduction of any investment management fees which would reduce returns and assume reinvestment of all distributions. Investment in the fund is not available on a fee free basis and this should be factored into any analysis of past performance.

Net returns as at 30 April 2021

	From 17 December 2015	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception^ % p.a.
Yarra Australian Real Assets Securities Fund	7.92	2.61	5.48	14.71	7.58	6.26	8.37	7.41
S&P/ASX Custom Infrastructure, Utilities and A-REITs Index*	7.25	2.65	5.35	15.13	5.89	5.81	NA	NA
Excess Return†	0.67	-0.05	0.13	-0.42	1.69	0.46	NA	NA
Growth Return‡	NA	NA	NA	2.43	-11.53	-8.93	-1.49	-0.75
Distribution Return‡	NA	NA	NA	12.28	19.11	15.19	9.86	8.16

Past performance is not a reliable indicator of future performance. Taxes payable by investors have not been taken into account. The figures shown have been provided for illustrative purposes – they are unaudited and subject to change. The total returns shown are prepared on an exit to exit basis – they include all ongoing fees and expenses and assume reinvestment of all distributions.

^ Inception date of Yarra Australian Real Assets Securities Fund: December 2005.
* Effective 17 December 2015, the benchmark for the Yarra Australian Real Assets Securities Fund is the S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index: a market cap weighted index of infrastructure, utilities and REIT securities included in the S&P/ASX300.
† Excess return: The excess return figures shown represent the difference between the portfolio's return and the benchmark return.
‡The Growth Return is measured by the movement in the Fund's unit price, ex-distribution, and can be positive or negative as the unit price can fluctuate with changes in the underlying market value of the Fund's assets. The Distribution Return is the amount that is paid to unitholders by way of income distribution in a 12-month period. It does not include distribution amounts deemed as capital distributions.

Market review

Infrastructure and REITs supported Australian Real Assets in April, more than offsetting ongoing weakness in the Utilities sector.

The S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Accumulation Index returned 2.7% for the month, taking its 12-month return to +15.1%. Real Assets underperformed the broader equities market, with the ASX300 returning +3.7% during April.

Within Infrastructure & Utilities (+2.1%), gains in Transportation Infrastructure (+3.7%) offset declines in Utilities (-1.2%) and Road & Rail (-3.8%). Toll road operator Transurban (TCL, +6.4%) outperformed after its third-quarter traffic update showed a recovery in its Australian roads amid easing travel restrictions, with management noting monthly improvements and more city-bound traffic. AGL Energy (AGL, -7.5%) declined after announcing the surprise resignation of its chief executive, effective immediately. Aurizon (AZJ, -3.8%) announced weaker coal volumes in 3Q21 as a result of weaker coal demand from customers, the end to one of its contracts, and weather disruption.

Within REITs (+3.1%), corporate activity picked up during April, with Blackstone selling its Milestone portfolio for $3.8bn and Centuria Capital (CNI, +x.x%) announcing a merger with Primewest in a $600mn deal. Residential-exposed REITs Stockland Group (SGP, +6.4%) and Mirvac Group (MGR, +7.6%) outperformed after announcing better-than-expected trading updates. SGP guided to the top end of its previous range and MGR upgrading underlying earnings guidance by 8% as Australian housing approvals continued to rise despite reduced government support.

Portfolio review

Key Contributors

AGL Energy (AGL, underweight) – the energy company underperformed after announcing the surprise resignation of its chief executive, effective immediately. The announcement creates significant uncertainty, given the company's recently communicated plans to split its coal generation and retail-facing businesses into separate entities. We remain underweight AGL. Whilst we support the strategic logic of demerging coal generation from its energy retailing business, the reality is that the dis-synergies of doing so will mean that neither of the two resulting businesses have much debt capacity, suggesting additional equity will be required to support the demerger.

Aurizon Holdings (AZJ, underweight) – the rail freight operator underperformed after announcing weaker coal volumes in 3Q21 as a result of weaker coal demand from customers, the end to one of its contracts and weather disruption. We are underweight AZJ because we find the headline valuation unsupportive (at an EV/EBITDA of 7.3 times and on a 12-month forward dividend yield of 7.5%) when considering long-term revenue headwinds. We believe the outlook for customer end markets in coal will weaken further, with the commodity facing structural challenges as the world's energy mix shifts away from emissions-intensive fossil fuels.

Scentre Group (SCG, underweight) – the retail REIT underperformed without any materially negative news during the period. Our underweight position is predicated on SCG's unsustainable balance sheet on a longer-term view, as asset values continue to move lower. Further, SCG is taking a tougher stance on negotiations with its non-SME tenants, which we believe increases vacancy risks across the portfolio. We do not regard SCG's forecast dividend yield of 5.3% as attractive versus peers given these risks. Our preferred Retail REIT exposure remains Vicinity (VCX), which offers a more compelling valuation and exposure to a recovering, Victorian-skewed portfolio.

Key Detractors

Vicinity Centres (VCX, overweight) – the retail REIT underperformed without any materially negative news during the period. We remain overweight the stock. While we continue to believe that shopping mall REITs face accelerated structural issues, we now believe this is well understood with VCX trading at 0.70 times trailing NTA. Due to its large exposure to Victoria (53% NTA), we expect short-term support as the state eases lockdown restrictions. Further, VCX's balance sheet can withstand further disruption and asset value moderation following the $1.4bn equity raising in June 2020, with gearing falling to 25%.

Stockland Group (SGP, underweight) – the diversified REIT outperformed after announcing a better-than-expected 3Q21 trading update. Management reaffirmed FFO guidance at the top end of its 32.5-33.1 cents per share range amid strong residential sales and improving retail rent collections (increasing to 94% net of abatements FYTD). Our underweight position remains premised on long-term concerns regarding SGP's asset values beyond COVID-19. Further, we remain concerned at the sustainability of current booming residential conditions which have been driven by pandemic-related stimulus programs, heavily supporting the first home buyer segment.

Charter Hall Group (CHC, underweight) – the fund manager REIT outperformed after upgrading operating EPS guidance to >57 cents per share, up from >55 cents per share. We remain underweight the stock based on our view that AUM growth and transaction volumes – which are running at elevated levels – will normalise in the medium term as the cap rate compression cycle slows. As the growth rate of the business slows from impressive double-digit levels, we expect the multiple to contract, putting pressure on the share price outlook. Within the real estate fund manager space, we maintain a preference for Centuria Capital (CNI).

Key Purchases

Qube Logistics (QUB) – we increased our position in the logistics company during the period. Assuming the Moorebank transaction occurs at end of 2021 as expected (the deal is non-binding at this stage), QUB's balance sheet will be returned to investment grade (at 2.5 times net debt to EBITDA) with the potential for a special dividend or buy-back. QUB's capex burden will also reduce from $1-1.2bn to $200-250mn, significantly improving the company's FCF profile. Lastly, we see further upside to QUB's Operating Division given strong levels of domestic economic activity and strong trading conditions for commodities and agriculture.

Charter Hall Social Infrastructure REIT (CQE) – we increased our position in the child care centre REIT during the period. We see CQE as well positioned to benefit from the re-opening Australian economy, with participation rates to normalise as lockdown measures are eased. CQE has a well-diversified portfolio of 410 centres, anchored by larger tenants (top-5) that pay 76% of its net operating income. Its lease terms are attractive, with a 12.7-year average duration, <5% expiring within the next 5 years and rent increasing by a prescribed amount each year. Further, its balance sheet is solid, with gearing (debt/assets) at 18%, and we regard its valuation as supportive (at 1.07 times NTA).

Key Sales

Sydney Airport (SYD) – we increased our underweight to the airport operator due to the outlook for a more protracted recovery in international travel, underappreciated risks arising from airline and tenant agreements and the prospect of higher interest rates in the long term. Most airline agreements are scheduled for renewal in July 2021 which, if they are not extended, may result in adverse pricing outcomes for the airport operator. While we continue to view SYD's assets as high-quality and with strong barriers to entry, we regard the stock as fully valued at a normalised EV/EBITDA of 18.0 times when considering these risks.

APA Group (APA) – we reduced our position in the gas pipeline operator to fund other opportunities. That being said, APA remains a high-conviction overweight in the portfolio. Our positive view is premised on APA's valuation – at an EV/EBITDA of 12.6 times and with a 5.3% forecast dividend yield – which we view as attractive when considering its exposure to important gas markets and dominant market share position. In the medium term, we see dividend upside driven by lower funding costs, scope for a higher payout ratio, and a conservative balance sheet position.

Atlas Arteria (ALX) – we trimmed our position in the toll road operator but maintain a high-conviction overweight position based on its strong liquidity and balance sheet position, which leaves it well placed to weather the COVID-19 related downturn in revenues, and a positive long-term view. ALX holds attractive, long-duration assets and trades at a discounted valuation (11 times normalised EV/EBITDA), which more than captures the disruption from COVID-19 as travel restrictions and lockdowns reduce traffic volumes in the short term. We continue to believe the intrinsic value of ALX's assets will eventually be realised following the simplification of its ownership structure in the past two years, resulting in significant upside.

Key Active Overweights

GPT Group (GPT) – we believe GPT offers investors exposure to a high-quality, diversified commercial real estate portfolio. Its conservative balance sheet (gearing at 25%) and high level of liquidity ($1.2bn) provide us with confidence that the company is well positioned for the forthcoming de-valuation cycle. Lastly, GPT's valuation has become more attractive at 0.83 times trailing NTA, which implies a 13% fall in gross asset values – a more significant fall than our base expectations of 5-10% as a result of the COVID-19 crisis.

APA Group (APA) – our overweight position is based on our view that APA's valuation – at an EV/EBITDA of 12.6 times and with a 5.3% forecast dividend yield – is attractive when considering its exposure to increasingly important gas markets and dominant market share position. In the medium term, we see dividend upside driven by lower funding costs, scope for a higher payout ratio and a conservative balance sheet position.

Mirvac Group (MGR) – our investment thesis is premised on several factors. Firstly, we expect active residential development earnings (~17% of expected earnings in FY21) to rebound in FY22 and FY23, driven by improved lot volumes. Secondly, we view MGR's office portfolio (61% of its passive portfolio) as best-in-class in the A-REIT sector. Weighted average lease expiries (WALEs) are at 6.5 years, significantly longer than peers including GPT Group (GPT, 5.5 years) and Dexus Property (DXS, 4.5 years). Lastly, we do not believe its strong overall growth profile (~10% EPS growth in FY22 and FY23) is captured in its current valuation, trading at 1.04 times trailing NTA.

Key Active Underweights

Stockland (SGP) – our underweight position is premised on long-term concerns about SGP's asset values beyond COVID-19 and the sustainability of current booming residential conditions driven by pandemic-related stimulus programs, heavily supporting the first home buyer segment currently. SGP's valuation faces downside risk given its exposure is to second-tier shopping centres (43% of NTA), where structural change is likely to accelerate, and to residential (22% of NTA), where we see softer demand in the medium-term as the housing stimulus (HomeBuilder) rolls over and the impact of lower migration levels takes hold.

Scentre Group (SCG) – our underweight position is predicated on SCG's unsustainable balance sheet on a longer-term view, as asset values continue to shift lower. While headline gearing fell from 38% to 27.7% during the period as a result of the company issuing hybrid securities, we expect 10% further de-valuations in the next 6 to 18 months. Further, SCG is taking a tougher stance on negotiations with non-SME tenants, which we expect may lead to increased vacancy risks across the portfolio. Lastly, we do not see SCG's forecast dividend yield of 5.3% as attractive compared to peers given these risks. Our preferred Retail REIT exposure remains Vicinity (VCX), which offers a more compelling valuation and exposure to a recovering, Victorian-skewed portfolio.

Aurizon Holdings (AZJ) – we are underweight AZJ because we find the headline valuation unsupportive (at an EV/EBITDA of 7.3 times and on a 12-month forward dividend yield of 7.5%) when considering long-term revenue headwinds. We believe the outlook for customer end markets in coal will weaken further, with the commodity facing structural challenges as the world's energy mix shifts away from emissions-intensive fossil fuels.

Market outlook

We maintain our conviction in the Real Assets sector, underpinned by solid fundamentals and attractive underlying valuation support. The S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Accumulation Index offers a 12-month forward forecast dividend yield of 4.1%, a compelling 2.5% premium above the 10-year Australian bond rate.

Within Infrastructure, we believe that in the long run strong fundamentals and attractive growth opportunities should continue to support the likes of Transurban (TCL) and Atlas Arteria (ALX). In the nearer term we expect toll roads to be at the forefront of the post COVID-19 recovery as activity amongst patronage-based infrastructure assets rebounds. We remain cautious towards infrastructure providers with exposure to cyclical end markets such as AGL Energy (AGL) with a strong preference within Utilities for APA Group where we see substantial scope for operating cash flow growth and higher dividends over the medium term.

Within A-REITs, we maintain a strong preference to being exposed to high quality asset owners with strong balance sheets at more attractive valuations such as GPT Group (GPT). We believe the structural headwinds facing shopping mall owners are likely to persist – changing consumer preferences are directing an increasing proportion of retail sales away from malls to online – and we continue to maintain a highly selective approach across the sector, steering away from owners of malls lacking strong competition barriers and steering towards resilient sectors with attractive long-term leases (10-years+) and high quality tenants.

We expect patches of short term uncertainty for earnings and distributions will remain in place as the COVID-19 recovery continues, as tenants exposed to the Australian consumer and SME customer are faced with escalating operating constraints. Robust balance sheets (average gearing levels around 25% net debt / total assets), solid levels of liquidity and strong in-place occupancy levels suggest that, overall, REITs are well positioned to see through the current dislocation.

Sector allocation

	Portfolio %	Benchmark %	Active %
Infrastructure	**36.39**	**34.12**	**2.27**
Airport Services	5.33	7.67	-2.34
Highways & Railtracks	23.93	18.86	5.07
Communication Services	0.00	1.98	-1.98
Railroads	0.00	2.94	-2.94
Marine Ports & Services	5.52	2.66	2.85
Information Technology	1.61	0.00	1.61
Utilities	**9.24**	**10.46**	**-1.22**
Electric Utilities	0.00	3.10	-3.10
Gas Utilities	9.24	5.01	4.23
Multi-Utilities	0.00	2.35	-2.35
Real Estate Investment Trusts (REITs)	**54.09**	**55.42**	**-1.33**
Specialized REITs	6.13	2.65	3.48
Diversified REITs	19.48	18.68	0.80
Industrial REITs	13.12	14.32	-1.20
Office REITs	1.83	5.95	-4.12
Retail REITs	11.52	12.69	-1.17
Other	1.99	1.13	0.87
Cash and receivables	**0.29**	**0.00**	**0.29**

Top 5 holdings

	Portfolio %	Benchmark %	Active %
Transurban	18.15	16.41	1.74
Goodman	13.12	13.45	-0.32
APA	9.24	5.01	4.23
Mirvac	8.39	4.48	3.91
GPT	8.33	3.81	4.52

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
GPT	8.33	3.81	4.52
APA	9.24	5.01	4.23
Mirvac	8.39	4.48	3.91
Underweights			
Stockland	0.00	4.72	-4.72
Scentre	2.84	5.97	-3.13
Aurizon	0.00	2.94	-2.94

Portfolio holdings may not be representative of current or future investments. The securities discussed may not represent all of the portfolio's holdings and may represent only a small percentage of the strategy's portfolio holdings. Future portfolio holdings may not be profitable.

Features

Investment objective	To achieve a balance of income and medium-to-long term capital growth by investing primarily in Australian listed infrastructure, utilities and REIT securities. In doing so, we aim to outperform the S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index over rolling three year periods.	
Recommended investment time frame	5 - 7 + years	
Fund inception	December 2005	
Fund size	A$24.1 mn as at 30 April 2021	
APIR code	JBW0030AU	
Estimated management cost	0.85% p.a.	
Buy/sell spread	+/- 0.15%	
Platform availability	Asgard BT Panorama BT Wrap Hub24 IOOF Pursuit Select Macquarie Wrap Consolidator	OneVue PowerWrap SmartWrap

Applications and contacts

Investment into the Yarra Australian Real Assets Securities Fund can be made by Australian resident investors only.

Website www.yarracm.com

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