

# Yarra Australian Real Assets Securities Fund

## Gross returns as at 31 January 2023

	From 17 December 2015	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception <sup>^</sup> % p.a.
Yarra Australian Real Assets Securities Fund	8.33	5.59	8.82	4.50	0.85	7.72	9.15	8.16
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index <sup>*</sup>	7.38	5.66	9.33	3.41	0.54	6.38	NA	NA
Excess Return <sup>†</sup>	0.95	-0.07	-0.51	1.09	0.30	1.34	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 31 January 2023

	From 17 December 2015	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception <sup>^</sup> % p.a.
Yarra Australian Real Assets Securities Fund	7.42	5.51	8.59	3.62	0.00	6.82	8.23	7.25
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index	7.38	5.66	9.33	3.41	0.54	6.38	NA	NA
Excess Return <sup>†</sup>	0.04	-0.15	-0.74	0.21	-0.55	0.43	NA	NA
Growth Return <sup>‡</sup>	-8.50	5.51	6.89	-21.21	-13.96	-11.22	-4.26	-2.05
Distribution Return <sup>‡</sup>	15.92	0.00	1.69	24.83	13.96	18.04	12.49	9.30

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.

<sup>^</sup> Inception date of Yarra Australian Real Assets Securities Fund: December 2005.

<sup>\*</sup> 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.

<sup>†</sup> Excess return: The excess return figures shown represent the difference between the portfolio's return and the benchmark return.

<sup>‡</sup> 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

The custom Infrastructure, Utilities and A-REITs Accumulation Index gained +5.7% for the month, taking its 12-month return to +3.4%. The broader ASX300 mirrored, gaining +6.3% for the month, as did global indices (MSCI World Index +7.1%).

All A-REIT sub-sectors recorded positive performance during the month, however there was significant performance divergence at the sub-sector and stock level. The Industrial sub-sector returned +14.5%, Diversified +8.5%, Office returned +5.7%, Residential +3.4% and Retail +4.4%. Key Outperforming A-REITs were Unibail (URW, +17.9%), Goodman Group (GMG, +15.0%) and Charter Hall (CHC, +14.9%). Key underperforming A-REITs were largely at the smaller end and included Arena REIT (ARF, -2.6%), Hotel Property Investment (HPI, -1.4%) and Region Group (RGN, -0.4%).

### Portfolio review

#### Key Contributors

**APA Group (APA, underweight)** – the gas pipeline operator underperformed during the month on limited news flow outside the appointment of Adam Watson, the company's prior CFO, as its new chief executive. We remain underweight the company given its difficult starting point in approaching the energy transition. In our view, APA's initiatives to shift its business model towards electrification will prove insufficient.

**AGL Energy (AGL, underweight)** – the energy company underperformed during the month despite an upgrade from competitor Origin Energy in their Energy Markets division. Following a tumultuous two years, AGL continues to face significant uncertainties in its outlook. The company faces significant challenges protecting its earnings base and fund investment in new generation assets as its highly profitable coal generation fleet is gradually retired over the next decade.

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**Aurizon (AZJ, underweight)** – the rail freight operator underperformed during the month on limited news flow. The portfolio retains an underweight position in Aurizon due to the difficulties the company faces and lack of genuine progress in transitioning its business model away from coal haulage.

### **Key Detractors**

**Goodman Group (GMG, underweight)** – our underweight position in the industrial property developer detracted from portfolio returns as fund managers such as GMG rallied strongly in January in-line with the large movement (lower) in bond yields. Property fund managers typically act as the longer duration cohort. Results from global peers released during the period also supported aspects of the global logistics outlook (positive rental reversions). We shifted underweight in the industrial property developer in late 2022 to reflect our expectation of slower earnings growth for the business, driven by the implications of the cap rate cycle turning higher for industrial assets and development activity and returns slowing from peak levels. While we believe GMG remains well placed to continue to grow earnings well above sector peers (FY23 EPS guidance is currently for +11% y/y, conservative in our view), we have recalibrated our expectations given an elevated valuation (21 times 12-months forward earnings) and modest 1.5% dividend yield.

**Charter Hall (CHC, underweight)** – our underweight position in the fund manager REIT detracted from portfolio returns as property fund managers – including CHC – rallied strongly in January in-line with the large movement (lower) in bond yields. We remain underweight the stock owing to concerns of lower equity flows into existing unlisted funds – wholesale and retail – as commercial valuation declines accelerate into CY23. Additionally, almost 40% of CHC's total FUM resides in the office sub-sector, which is likely to see the largest headwinds (income growth, valuation declines). Notwithstanding an already de-rated P/E of approximately 16 times, we believe these headwinds are yet to be fully factored into earnings expectations.

**Hotel Property Investments (HPI, overweight)** – the pub owner detracted from portfolio returns as company's share price took a pause following a very strong December, when expectations of potential M&A activity with 360 Capital drove the share price higher. REIT investors are familiar with 360 Capital's strategy and their past investment approaches in the REIT space, which at times have led or contributed to an unlocking of greater value (Irongate Group a recent example). We remain overweight HPI, with the company now trading at 0.87 times its last stated NTA and offering a 5.3% dividend yield.

### **Key Purchases**

There were no key purchases during the period.

### **Key Sales**

There were no key sales during the period.

### **Key Active Overweights**

**GPT Group (GPT)** – we believe GPT offers investors exposure to a high-quality, diversified commercial real estate portfolio. The company's conservative balance sheet (gearing at <30%) and high level of liquidity provide us with confidence that the company is appropriately positioned for the forthcoming devaluation cycle. Lastly, GPT's valuation is attractive at 0.74 times trailing NTA and 5.4% dividend yield.

**Chorus (CNU)** – the quality regulated utility trades on a 5.8% FY24 dividend yield with medium term upside in regulatory returns. As the build out of CNU's fibre network comes to an end, CNU will move to strong free cash flow generation with a balance sheet that is under levered vs target gearing and strong line of sight on regulatory revenues. Based on current market metrics, CNU would earn a 100bp higher regulatory return in the next regulatory period from July 2024, providing further upside to the medium-term dividend yield.

**Centuria Industrial REIT (CIP)** – we view the industrial asset class as more resilient than other sub-sectors moving into CY23. This was demonstrated by CIP's 31 Dec 2022 valuations which saw the portfolio value drop by less than 2%, demonstrating the high-quality asset-asset base (average lease tenure 8+ years, capital city locations). Additionally, the December result revealed very strong rental growth (re-leasing spreads of +19% in the 1H23 period) helping to offset the company's rising cost of debt. Meanwhile, the stock is trading at a 17% discount to updated NTA, an attractive investment proposition in our view.

### **Key Active Underweights**

**APA Group (APA)** – we remain underweight the gas pipeline operator on the grounds that APA's initiatives to shift its business model towards electrification will prove insufficient. We expect the company will be dwarfed by the discount increasingly applied to its gas pipeline business, particularly as planned government policies accelerate the shift to zero emissions sources. As a result, we no longer see its valuation (at a 12-month EV/EBITDA of 12.9 times) as sufficiently compelling when compared to large cap infrastructure alternatives.

**Stockland (SGP)** – our underweight position in the diversified REIT is premised on long-term concerns about the sustainability of what is now becoming the tail-end of booming domestic residential conditions driven by pandemic-related stimulus programs, which has heavily supported the first home buyer segment. Over time, SGP's valuation faces downside risk given its exposure to second-tier shopping centres (approximately 40% of NTA), where structural change is likely to accelerate, and to residential profitability (34% earnings, and 20% 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.

**Goodman Group (GMG)** – the underweight position reflects our expectation of slower earnings growth for the business, driven by the implications of the cap rate cycle turning negative for industrial assets, and development activity and returns slowing from peak levels. While we believe GMG

remains well placed to continue to grow earnings well above sector peers (FY2023 EPS guidance is currently for +11% y/y, conservative in our view) we have recalibrated our expectations given an elevated P/E of 21 times 12-months forward and offering a modest 1.5% dividend yield.

## Market outlook

We maintain our longer-term 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 4.6%, an attractive 0.9% premium above the 10-year Australian bond rate with the index dividend yield to increase in future years as traffic levels normalise on patronage-based infrastructure assets.

We see opportunities in high quality infrastructure companies with strong inflation protection. Chorus (CNU), for example, has now fully bedded down its regulatory regime and has a healthy dividend yield of 5.8% which we expect to grow through the remainder of the decade. We remain cautious towards utilities names with a high reliance on fossil fuels and difficulty in transitioning to a lower carbon environment namely AGL Energy (AGL) and APA Group (APA).

We see a mixed outlook across REIT sub-sector exposures heading into CY23. Positively, we see industrial fundamentals as favourable, as ongoing occupier demand outstrips supply, supporting significant real rental growth. Office and retail sub-sectors face more challenged conditions in our view, as the work-from-home dynamic continues to constrain office leasing demand, and retailers face moderating conditions as higher interest rates impact consumer spending. Pleasingly in the current environment, a number of the REITs have rents linked to CPI increases, providing an effective hedge to increasing inflation.

The calendar year ahead is, however, likely to see higher interest rates place downward pressure on capital values (i.e. REIT NTA vulnerability, following the sector growing average NTA by +3.8% in the June-22 half). We believe much of this concern is built into REIT share prices, however, which are trading materially below NTA's. Indeed, 1H23 valuations released in December for some A-REITs reflected an average cap rate softening of 18 bps (~4% decline in asset values). In this environment, we believe there is a heightened importance to maintain portfolio exposures to preferred sub-sectors and to those REITs with sustainable balance sheets that can navigate the period to come, continuing to generate attractive dividends for investors.

## Top 5 holdings

	Portfolio	Benchmark	Active
Transurban	18.70	18.33	0.37
Goodman	11.75	14.75	-2.99
GPT	7.93	3.76	4.17
Origin Energy	6.82	5.55	1.27
Mirvac	5.86	3.87	1.99

## Key active positions

Overweights	Portfolio	Benchmark	Active
GPT	7.93	3.76	4.17
Chorus	4.26	1.48	2.77
Centuria Industrial REIT	3.38	0.78	2.61
Underweights			
APA	0.00	5.38	-5.38
Stockland	0.00	4.05	-4.05
Goodman	11.75	14.75	-2.99

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.

## Sector allocation

	Portfolio	Benchmark	Active
<b>Infrastructure</b>	<b>34.86</b>	<b>30.01</b>	<b>4.84</b>
Airport Services	1.54	0.79	0.75
Highways & Railtracks	20.32	21.94	-1.61
Communication Services	5.10	1.75	3.35
Railroads	0.00	2.93	-2.93
Marine Ports & Services	5.69	2.60	3.09
Information Technology	2.19	0.00	2.19
<b>Utilities</b>	<b>6.82</b>	<b>12.91</b>	<b>-6.09</b>
Electric Utilities	6.82	5.55	1.27
Gas Utilities	0.00	5.38	-5.38
Multi-Utilities	0.00	1.98	-1.98
<b>Real Estate Investment Trusts (REITs)</b>	<b>56.08</b>	<b>57.08</b>	<b>-0.99</b>
Specialized REITs	4.78	3.70	1.08
Diversified REITs	13.79	17.23	-3.44
Industrial REITs	15.14	15.81	-0.67
Office REITs	5.46	4.70	0.76
Retail REITs	15.02	14.92	0.10
Other	1.91	0.73	1.18
<b>Cash and receivables</b>	<b>2.24</b>	<b>0.00</b>	<b>2.24</b>

## 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\$17.7 mn as at 31 January 2023	
APIR code	JBW0030AU	
Estimated management cost	0.85 p.a.	
Buy/sell spread	+/- 0.15	
Platform availability	Asgard BT Panorama	Hub24

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## Applications and contacts

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

**Website** [www.yarracm.com](http://www.yarracm.com)

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