Yarra Australian Real Assets Securities Fund

Gross returns as at 31 March 2022

	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	9.44	3.11	-4.30	14.89	6.10	8.24	10.15	8.58
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index*	8.71	3.78	-2.17	19.17	5.39	7.19	NA	NA
Excess Return†	0.73	-0.67	-2.13	-4.27	0.71	1.04	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 March 2022

	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	8.52	3.03	-4.50	13.93	5.20	7.32	9.23	7.67
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index	8.71	3.78	-2.17	19.17	5.39	7.19	NA	NA
Excess Return†	-0.19	-0.75	-2.33	-5.24	-0.18	0.13	NA	NA
Growth Return‡	NA	NA	NA	6.84	-6.81	-8.58	-1.04	-0.46
Distribution Return‡	NA	NA	NA	7.09	12.02	15.90	10.27	8.13

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

Australian Real Assets declined in the March 2022 quarter, underperforming the wider market as high inflation spurred Federal Banks to accelerate quantitative tapering and to begin interest rate hikes.

The S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Accumulation Index declined by 2.2% during the quarter, compared to the wider ASX300 which returned +2.1% amid strong performances from the Banking and Resources sectors. Globally, equities declined (S&P500 -4.6%) as US real yields rose, with the US 10-year Treasury Inflation-Protected Securities (TIPS) climbing 52 bps to -0.58% as the US Fed raised its target rate to 0.25-0.5% and signalled many more to come.

Within Infrastructure & Utilities (+4.1%), Utilities supported the benchmark while Transportation Infrastructure was flat. At a stock level, multi-utility provider AGL Energy (AGL, +28.4%) rallied in response to a better-than-expected 1H22 result, higher wholesale electricity prices and after receiving a takeover offer from a Brookfield consortium, which was ultimately rejected. Elsewhere, gas pipeline operator APA Group (APA, +6.1%) also delivered a solid result, with management highlighting that most of the company's revenue is linked to inflation.

Within REITs (-6.7%), Retail and Office REITs outperformed the sector as COVID cases appeared to have peaked across the east coast of Australia, while Industrial and Diversified REITs underperformed. At a stock level, shopping mall owner Vicinity Centres (VCX, +13.1%) delivered results ahead of expectations as operating conditions improved. Conversely, Industrial REIT Goodman Group (GMG, -13.6%) underperformed despite delivering a strong 1H22 result, with operating EPS 12% ahead of consensus, reflecting elevated market expectations and a high earnings multiple in a period of rising interest rates.

Portfolio review

Key Contributors

Charter Hall Group (CHC, underweight) – the fund manager REIT underperformed amid concerns around higher real yields. The company also released its 1H22 result, with EPS below consensus forecasts for the period but full-year guidance upgraded by 7%. 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, our preferences are in Goodman Group (GMG) and Centuria Capital (CNI).

Vicinity Centres (VCX, overweight) – the shopping mall REIT outperformed as omicron cases across the east coast of Australia appeared to have peaked and after delivering a better-than-expected 1H21 result. Funds from operations (FFO) came in at $287mn, supported by the reversal of waivers and provisions from the prior year. We remain overweight the stock. While we continue to believe that shopping mall REITs face accelerated structural issues, we now believe this is well recognised with VCX trading at 0.82 times trailing NTA, and increasing direct transactional evidence at prices at or close-to prevailing NTA's. Due to its large exposure to Victoria (53% NTA), we expect short-term support as the state emerges from a high number of COVID cases.

Chorus (CNU, overweight) – the company outperformed following a better-than-expected 1H22 result and better than anticipated medium term dividend guidance. 1H22 EBITDA came in at $332mn, modestly ahead of expectations, while full-year guidance was increased to $660-685mn and dividend guidance for FY22, FY23 and FY24 was increased to 35, 40 and 45 cents per share respectively. We remain overweight. The regulatory regime for CNU – which had caused prior uncertainty with the stock – has now been largely settled and has commenced from the start of the year. The stock offers attractive attributes of regulated returns and modest growth on the appealing valuation metrics of a 5.4% dividend yield and 8.4 times EV/EBITDA. With peer companies trading on much higher multiples in New Zealand and medium-term regulatory return upside, we expect the stock to re-rate as the market becomes comfortable with CNU's regulatory model.

Key Detractors

Origin Energy (ORG, overweight) – the energy company outperformed as oil prices increased (with Brent Crude rising 46% to US$113/bbl), the outlook for higher electricity prices domestically and in response to a strong 2QFY22 result. LNG prices were ahead of expectations, averaging US$11.80/mmbtu during the period, while production was solid due to planned maintenance completing ahead of schedule. We remain underweight the company given its heavy reliance on Energy exposure to generate cash flow through its 27.5% stake in vertically integrated LNG export terminal APLNG. ORG has announced the closure of its Eraring coal power plant which we view positively, given it positions the company as capital light participant in the energy transition with a large retail customer base.

AGL Energy (AGL, underweight) – the utilities company rallied in response to a better-than-expected 1H22 result, higher wholesale electricity prices and after receiving a takeover offer from a Brookfield consortium, which was ultimately rejected. Underlying NPAT for the period was more than 60% ahead of analyst forecasts as AGL benefited from large competitor generation outages in both Victoria and Queensland. We remain underweight AGL. While we support the strategic logic of demerging its coal generation business 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 material debt capacity, suggesting additional equity may be required to support the demerger.

Centuria Capital Group (CNI, overweight) – the fund manager REIT underperformed amid concerns around higher real yields resulting in lower capacity to maintain FUM growth at elevated levels, which more than offset a 1H22 result above consensus forecasts. Notwithstanding this potential headwind to CNI's valuation, we continue see CNI's growth platform as attractive. The company manages a diversified portfolio by property asset type and capital source, underpinned by listed investment vehicles (CIP and COF). We hold a positive view of its recent merger with Primewest Group (PWG) which increases CNI's FUM to $17bn, is accretive and diversifies the business across new markets (Retail, Agriculture). The company trades on a 12-month forward P/E of 17.7 times which, while above peer Charter Hall Group (CHC, at 16.1 times), is justified given CNI's superior medium-term growth potential.

Key Purchases

Vicinity Centres (VCX) – we increased our position in the shopping mall REIT, where we continue to see upside as Australia emerges from the COVID crisis. While we continue to believe that shopping mall REITs face accelerated structural issues, we now believe this is well recognised with VCX trading at 0.82 times trailing NTA, and increasing direct transactional evidence at prices at or close-to prevailing NTA's. Due to its large exposure to Victoria (53% NTA), we expect short-term support as the state emerges from a high number of COVID cases.

Qube Logistics (QUB) – we increased our position in the logistics company during the period. Following the Moorebank transaction, QUB's balance sheet has returned to investment grade (at 2.5 times net debt to EBITDA) with the company announcing a $400m buy-back. QUB's capex burden has also reduced from $1-1.2bn to $200-250mn, significantly improving the company's FCF profile. We see further upside to QUB's Operating Division as supportive trends drive higher consumer and housing activity in Australia and expect strong trading conditions in the Ports and Bulk division to persist amid high export volumes in resources and agricultural trade.

Chorus (CNU) – we increased our position in the communications infrastructure company. The regulatory regime for CNU – which had caused prior uncertainty with the stock – has now been largely settled and has commenced from the start of the year. The stock offers attractive attributes of regulated returns and modest growth on the appealing valuation metrics of a 5.4% dividend yield and 8.4 times EV/EBITDA. With peer companies trading on much higher multiples in New Zealand and medium-term regulatory return upside, we expect the stock to re-rate as the market becomes comfortable with CNU's regulatory model.

Key Sales

Sydney Airport (SYD) – the airport operator exited the ASX following the successful takeover led by the IFM and GIP consortium. We held a benchmark position in the company, reflecting our view the latest takeover offer for the company fully reflected its recovery at $8.75 per share and, at an EV of 23 times CY19 earnings, was above other major airport transactions globally.

Centuria Capital Group (CNI) – we reduced our overweight position as concerns around higher real yields resulted in lower capacity to maintain FUM growth at elevated levels. That being said, we remain overweight the company as we continue to see its growth platform as attractive. The company manages a diversified portfolio by property asset type and capital source, underpinned by listed investment vehicles (CIP and COF). We hold a positive view of its recent merger with Primewest Group (PWG) which is accretive and diversifies the business across new markets (Retail, Agriculture). The company's P/E trades at of 18.4 times which, while above peer Charter Hall Group (CHC, at 16.2 times), is justified given CNI's superior medium-term growth potential.

Transurban (TCL) – we reduced our position in the toll road operator and are now modestly overweight. While we continue to believe TCL has a strong growth outlook (with a number of new project and expansion plans), its risk-adjusted total return potential is reduced in the current macro environment. While TCL is advantaged by toll-road revenues linked to CPI, this will largely be offset by the impact to its valuation from higher interest rates. Our preferred toll road exposure is Atlas Arteria (ALX), where we see greater valuation support particularly through concession extensions at APRR and settling the Dulles Greenway tolling regime.

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 more than a 15% fall in gross asset values – a more significant fall than our base expectations.

Vicinity Centres (VCX) – we continue to see upside in the shopping mall REIT as Australia emerges from the COVID crisis. While we continue to believe that shopping mall REITs face accelerated structural issues, we now believe this is well recognised with VCX trading at 0.82 times trailing NTA, and increasing direct transactional evidence at prices at or close-to prevailing NTA's. Due to its large exposure to Victoria (53% NTA), we expect short-term support as COVID cases across the state continue to fall. 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%.

BWP Trust (BWP) – we believe BWP trades at a compelling valuation versus peers – 1.1 times NTA (based on conservative cap rates) with a 4.6% forecast yield – when considering its strong operating outlook, driven by well-located properties that encourage high rates of lease renewals from tenant Bunnings. Further, the REIT is set to benefit from higher inflation given CPI leases account for around 53% of its lease structures.

Key Active Underweights

Origin Energy (ORG) – we remain underweight the company given its heavy reliance on Energy exposure to generate cash flow through its 27.5% stake in vertically integrated LNG export terminal APLNG. ORG has announced the closure of its Eraring coal power plant which we view positively, given it positions the company as capital light participant in the energy transition with a large retail customer base.

Stockland (SGP) – our underweight position is premised on long-term concerns about the sustainability of current booming residential conditions driven by pandemic-related stimulus programs, heavily supporting the first home buyer segment currently. Over time, 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 profitability (35% earnings, and 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.

APA Group (APA) – we remain underweight the company on the grounds that APA's initiatives to shift its business model towards electrification won't be sufficient. We expect it to 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 11.5 times) as sufficiently compelling when compared to large cap infrastructure alternatives.

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 1.3% 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 and exposure to recovering economies, qualities both present within the transportation infrastructure sector. Toll roads are at the forefront of the post COVID-19 recovery and in Atlas Arteria (ALX) we see several catalysts on the horizon for patient investors, with a generous dividend yield in the meantime (+6.2%). Qube Holdings has strong exposure to high volumes in Australia's consumer, agricultural and resources markets along with a demonstrated ability to offset any cost inflation through levies. 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 moving into CY2022. Positively, we see recovering occupier demand – particularly as office workers return to the offices, and shoppers return back to shopping malls – following an elongated period of Covid-disruptions and restrictions concentrated in the major cities of Melbourne and Sydney (combined >50% A-REIT asset exposure). We expect this to drive improved leasing outcomes and support the rent collection trajectory. Additionally, a number of the REITs also have rents linked to CPI increases, providing an effective hedge to increasing inflation. However, accompanying this recovery, we expect into CY22 the prospect of higher interest rates to begin to temper capital appreciation (i.e. REIT NTA growth) as investor acquisition return requirements stabilise and begin to increase, and REITs see an end of the multi-year trend of falling borrowing costs (an important driver of earnings and dividend growth over the past three years).

Top 5 holdings

	Portfolio %	Benchmark %	Active %
Goodman	18.21	15.71	2.50
Transurban	17.67	16.79	0.88
GPT	7.54	4.00	3.53
Vicinity Centres	6.39	2.91	3.47
Atlas Arteria	5.59	2.54	3.05

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
GPT	7.54	4.00	3.53
Vicinity Centres	6.39	2.91	3.47
BWP Trust	4.12	0.78	3.33
Underweights			
Origin Energy	0.00	4.43	-4.43
Stockland	0.00	4.11	-4.11
APA	1.44	5.08	-3.64

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 %
Infrastructure	**38.14**	**28.32**	**9.82**
Airport Services	0.00	0.67	-0.67
Highways & Railtracks	23.26	19.32	3.93
Communication Services	5.50	2.94	2.56
Railroads	0.00	2.74	-2.74
Marine Ports & Services	6.89	2.65	4.24
Information Technology	2.49	0.00	2.49
Utilities	**1.44**	**11.56**	**-10.12**
Electric Utilities	0.00	4.43	-4.43
Gas Utilities	1.44	5.08	-3.64
Multi-Utilities	0.00	2.05	-2.05
Real Estate Investment Trusts (REITs)	**57.25**	**60.12**	**-2.86**
Specialized REITs	5.54	3.92	1.62
Diversified REITs	13.31	18.74	-5.42
Industrial REITs	18.21	16.85	1.36
Office REITs	1.97	5.84	-3.87
Retail REITs	16.25	14.02	2.23
Other	1.97	0.75	1.22
Cash and receivables	**3.16**	**0.00**	**3.16**

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$19.4 mn as at 31 March 2022	
APIR code	JBW0030AU	
Estimated management cost	0.85% p.a.	
Buy/sell spread	+/- 0.15%	
Platform availability	Asgard BT Panorama	Hub24

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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