

Yarra Australian Real Assets Securities Fund

Gross returns as at 31 March 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 [†] % p.a.
Yarra Australian Real Assets Securities Fund	7.78	-3.38	3.05	-2.09	12.90	7.77	8.29	7.93
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index [*]	6.72	-3.89	2.15	-4.97	12.32	6.39	NA	NA
Excess Return [†]	1.06	0.51	0.90	2.89	0.58	1.38	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 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 [†] % p.a.
Yarra Australian Real Assets Securities Fund	6.87	-3.44	2.84	-2.91	11.95	6.86	7.38	7.02
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index	6.72	-3.89	2.15	-4.97	12.32	6.39	NA	NA
Excess Return [†]	0.15	0.44	0.68	2.06	-0.37	0.47	NA	NA
Growth Return [‡]	-8.64	-3.44	2.84	-26.18	-3.69	-11.18	-5.01	-2.17
Distribution Return [‡]	15.52	0.00	0.00	23.26	15.64	18.05	12.39	9.20

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 rallied during the March 2023 quarter, with all sub-sectors having positive returns.

The Custom Infrastructure, Utilities and A-REITs Accumulation Index returned +2.2% during the quarter, taking its 12-month return to -5.0%. In comparison, the broader ASX300 gained 3.3% for the quarter while, globally, the MSCI World Index climbed by 7.9%.

Portfolio review

Key Contributors

APA Group (APA, underweight) – the gas transmission pipeline network owner underperformed during the quarter in which it announced the appointment of its prior CFO, Adam Watson, as the company's new CEO and reported a result largely in line with expectations. Whilst a clearer strategy is emerging under

the new CEO, we remain underweight the stock given the company is at a difficult starting point in approaching the energy transition.

Aurizon (AZJ, underweight) – the freight rail transport company underperformed during the quarter, reporting weaker than expected earnings that were heavily impacted by weather related disruptions. The earnings weakness is also anticipated to carry into the second half of the financial year. The portfolio retains an underweight position, reflecting the difficulties it faces in transitioning its business model away from coal haulage and the associated capital intensity of this process.

Charter Hall Group (CHC, underweight) – our underweight position in the diversified commercial real estate fund manager, developer and owner added value over the period. The key driver of the underperformance was the growing expectation of looming property valuation weakness over CY23, reduced equity flows across the real estate platform and, subsequently, a slowdown in group earnings growth.

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Notwithstanding an undemanding headline valuation multiple today of 12.1-times forward P/E and offering a 4.6% dividend yield, we expect these issues will continue to create a headwind, and retain an underweight position.

Key Detractors

Stockland (SGP, underweight) – Australia’s largest land subdivision business, that typically sells approximately 6,000 land lots annually, outperformed over the period. Notwithstanding ongoing softness in residential demand for land lots, investors took a more optimistic view to look through current conditions, with some belief that residential conditions will begin to improve in the latter part of CY23 as expectations of interest rate cuts into CY24 begin to build. With elevated shorter-term earnings risk, and the stock trading now on fuller valuation metrics of 12.9-times forward earnings and offering a 6.4% dividend yield, we retain an underweight position. We maintain a preference for peer Mirvac insofar as residential exposure is concerned.

Charter Hall Social Infrastructure REIT (CQE, overweight) – our overweight position in the owner of a large and well diversified portfolio of childcare and other social infrastructure assets detracted from returns over the period. While the outlook for CQE is well supported by high occupancy, contracted rental growth on leases to its childcare and social infrastructure tenants, the stock weakened as valuation concerns grow across all long-leased (i.e. longer than 10-year average lease duration) commercial real estate assets in the higher interest rate environment. While CQE won’t be immune, we believe their assets will outperform owing to a degree of inflation linked rents, and a favourable fundamental demand/supply outlook for childcare assets underpinning growing rents.

Ingenia Communities (INA, overweight) – the share price of the affordable housing developer and owner fell following an earnings update that highlighted weaker operating conditions than first anticipated by the company. INA now assumes longer construction timeframes and slower settlements as a result of weakening residential conditions. While the balance sheet is sufficiently capitalised to support the operational weakness, the downgrade does highlight the short-term vulnerability in the business model and has adjusted earnings expectations accordingly.

Key Purchases

HomeCo (HMC) – we initiated a position in the diversified real estate funds management group during the period, via an opportunity to bid into a discounted equity raising associated with the acquisition of a portfolio of 11 Healthscope anchored healthcare assets. We like the outlook for the real estate asset mix underpinning HMC’s funds-growth (i.e. hospitals, large-format retail), the operational leverage – the business is expected to approach \$10bn of funds under management by the end of CY23 – and the attractive relative valuation compared to peer real estate funds management groups including Charter Hall and Centuria.

Transurban (TCL) – the portfolio increased its position in diversified toll road owner TCL during the period. TCL owns a high-quality portfolio of long concession length toll roads

geographically spread across Sydney, Melbourne, Brisbane and North America. TCL’s funding position remains very strong and distribution growth is set to accelerate as several expansion projects are commissioned. The stock trades on 23.5-times FY24 EV/EBITDA and a 4.3% dividend yield.

Chorus (CNU) – we increased our position in the high-quality regulated telecommunications utility during the period. CNU is the highest conviction infrastructure position in the portfolio, trading on a 5.8% FY24 dividend yield and with medium term upside in regulatory returns. As the build out of CNU’s fiber network comes to an end, the company will move to strong free cash flow generation, with a balance sheet that is under-levered vs target gearing and with strong line of sight on regulatory revenues.

Key Sales

WayPoint (WPR) – we completed the exit of our position in the service station owning REIT over the period. Our exit was predicated on our view of asset de-valuation risk through the cycle to come, following higher interest rates, and the expectation of cap rate expansion. From a longer-term perspective, there remains an open question on the ability of service stations to reposition themselves in the face of declining petrol demand from reduced combustion engine penetration rates. Within the specialised REIT space, our preference remains with childcare assets (via Charter Hall Social Infrastructure REIT) and high-quality, long-duration hotel leases (via Hotel Property Investments).

Charter Hall Retail (CQR) – we exited our position in the retail and service station owning REIT in the period. Through the cycle to come, we expect valuation cap rates on CQR’s assets to expand, lowering valuations, and bringing into focus balance sheet leverage, which is higher for CQR than its peers. Insofar as retail exposed REITs are concerned, our portfolio preferences sit with the diversified real estate GPT Group (owner of Melbourne Central), Vicinity Centres (owner of Chadstone, DFO outlets and a mix of other retail centres) and Bunnings Trust (owner of 60+ Bunnings anchored centres across the country).

Qube Holdings (QUB) – the portfolio reduced its holding in the logistics operator and stevedore owner during the quarter. With our thesis in QUB having largely played out, we chose to pivot into less cyclically exposed infrastructure owners, such as TCL and CNU.

Dexus (DXS) – we reduced further our position in Australia’s largest office landlord over the period. This decision was driven by our ongoing concern around the outlook (weak) for office operating metrics (lower rents), direct valuations as cap rates rise (lower valuations) and DXS’s development pipeline in this environment. With respect to office exposure, our preference is to gain exposure via our overweight in GPT Group, which also offers investors exposure to a recovering retail property portfolio (i.e. Melbourne Central) and a diversified industrial portfolio.

Key Active Overweights

GPT Group (GPT) – our overweight position the diversified commercial real estate owning REIT is predicated on asset quality (A-grade, prime assets) and mix (retail, industrial, office), robust balance sheet and undemanding stock valuation. Notwithstanding our expectation of sectorial downside risks to retail and office sub-sectors over CY23, we view the stock as attractive risk reward with modest gearing (29% LVR) and trading at a material discount to last stated NTA and offering an attractive 5.9% dividend yield.

Chorus (CNU) – the high-quality regulated telecommunications utility trades on a 5.8% FY24 dividend yield and with medium term upside in regulatory returns. As the build out of CNU's fiber 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 nearly 300bp 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 remain overweight the domestically focussed industrial owning REIT. We view the industrial asset class as more resilient than other sub-sectors as we progress through CY23. This was demonstrated by CIP's 31 Dec 2022 valuations which saw the portfolio value decline by less than 2%, demonstrating the high-quality 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 periods) which is helping to offset the rising cost of debt. Meanwhile, the stock is trading at an excessively steep discount to NTA, implying asset values will decline in excess of 15% from Dec 2022 valuations.

Key Active Underweights

APA Group (APA) – we remain underweight the energy company as we retain a cautious stance towards the heavy load of capital investment required to transition the business away from its core gas transmission activities. Whilst APA's gas pipelines will continue to provide an important role in facilitating energy flows across the east coast of Australia for many years to come, the quality of this business has diminished as contracted revenue tenor is increasingly short in duration relative to the very long dated nature of its assets.

Stockland (SGP) – we are underweight Australia's largest land subdivider, reflecting our expectations of the need for a recalibration of operating outcomes from the residential development side of the business, which we believe will deteriorate further over the year ahead. We would reassess the stock position in this environment, when default rates revert to higher levels (we expect they'll shift to 10%+, from 3% today) and expectations recalibrate accordingly. Outside of the residential exposure, we like the strategic direction under the stewardship of CEO Tarun Gupta, shifting the SGP business model to become more capital light. New partnerships with large global investors such as Mitsubishi Estate Asia, in our mind, validate the strategy.

Goodman (GMG) – while we continue to regard GMG as the global leader in industrial ownership, development and management, our underweight is premised on our view of where we sit in the real estate cycle. Specifically, higher interest rates are likely to result in slowing earnings growth (specifically from the development and management segments) and, subsequently, a lower stock multiple the market is prepared to pay. Adjusting to the environment, GMG has indicated it will seek to undertake more developments on its own balance sheet, which while a positive for activity, does carry an increased risk profile. Within the industrial sector, we have shifted funds to the more passive industrial player CIP, at this point in the cycle.

Market outlook

We expect real assets to play an important role across client portfolios in CY23 offering diversification benefits, defensive characteristics and favourable, regular inflation-protect income.

For the REITs, we see a mixed outlook across sub-sector exposures heading further into CY23. Positively, we see industrial and specialised-asset fundamentals (26% and 7% of sector assets respectively) as favourable: occupier demand continues to outstrip supply, supporting significant real rental growth. Office and retail sub-sectors (21% and 46% of sector assets respectively) face more challenged conditions in our view, as the work-from-home dynamic continues to constrain office leasing demand, while retailers face moderating conditions as higher interest rates impact consumer spending and the ongoing headwind from online growth. Pleasingly, in the current environment, a number of the REITs have rents linked to CPI increases, providing an effective hedge to increasing inflation.

However, CY23 is likely to see higher interest rates place upward pressure on capitalization rates (resulting in lower valuations). Remarkably, REIT valuations were broadly flat overall in the Dec-22 half, with rental growth offsetting 15bps of cap rate expansion. However, we believe much of this valuation concern is now built into REIT share prices which are trading materially below NTA's; passive REITs are trading in excess of 20% discounts to last NTA. We believe in this environment there is a heightened importance to maintain portfolio exposures to REITs with quality assets and sustainable balance sheets that can navigate the period to come, while continuing to generate attractive dividends for investors.

In terms of the Infrastructure & Utilities outlook, we see opportunities in high quality infrastructure companies with strong inflation protection. Chorus (CNU) 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 utility 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).

Top 5 holdings

	Portfolio	Benchmark	Active
Transurban	21.59	19.63	1.95
Goodman	11.54	14.45	-2.90
GPT	7.95	3.65	4.31
Origin Energy	7.90	6.42	1.48
Vicinity Centres	5.50	3.38	2.12

Key active positions

Overweights	Portfolio	Benchmark	Active
GPT	7.95	3.65	4.31
Chorus	5.27	1.55	3.72
Centuria Industrial REIT	3.60	0.73	2.87
Underweights			
Goodman	11.54	14.45	-2.90
Stockland	0.00	4.27	-4.27
APA	0.00	5.36	-5.36

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	36.41	31.15	5.26
Airport Services	1.70	0.87	0.83
Highways & Railtracks	22.64	23.08	-0.43
Communication Services	6.04	1.84	4.20
Railroads	0.00	2.78	-2.78
Marine Ports & Services	3.37	2.58	0.79
Information Technology	2.66	0.00	2.66
Utilities	7.90	13.95	-6.05
Electric Utilities	7.90	6.42	1.48
Gas Utilities	0.00	5.36	-5.36
Multi-Utilities	0.00	2.17	-2.17
Real Estate Investment Trusts (REITs)	34.29	30.06	4.23
Specialized REITs	2.33	2.72	-0.39
Diversified REITs	12.88	14.82	-1.95
Industrial REITs	3.60	0.98	2.62
Office REITs	3.92	4.42	-0.50
Retail REITs	9.74	6.49	3.25
Other	1.82	0.62	1.20
Cash and receivables	1.29	0.00	1.29

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\$17.0 mn as at 31 March 2023	
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.

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