

# Yarra Australian Real Assets Securities Fund

## Gross returns as at 30 September 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 <sup>^</sup> % p.a.
Yarra Australian Real Assets Securities Fund	6.14	-12.08	-7.90	-13.62	-2.73	4.79	8.33	7.27
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index <sup>*</sup>	5.04	-12.98	-9.39	-13.55	-3.49	3.29	NA	NA
Excess Return <sup>†</sup>	1.10	0.90	1.49	-0.08	0.76	1.50	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 September 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 <sup>^</sup> % p.a.
Yarra Australian Real Assets Securities Fund	5.24	-12.14	-8.10	-14.35	-3.55	3.90	7.41	6.36
S&P/ASX 300 Custom Infrastructure, Utilities and A-REITs Index	5.04	-12.98	-9.39	-13.55	-3.49	3.29	NA	NA
Excess Return <sup>†</sup>	0.20	0.84	1.29	-0.80	-0.06	0.62	NA	NA
Growth Return <sup>‡</sup>	NA	NA	NA	-34.39	-16.99	-13.66	-5.01	-2.95
Distribution Return <sup>‡</sup>	NA	NA	NA	20.04	13.44	17.57	12.42	9.31

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

Australian Real Assets declined during the September 2022 quarter, with all sectors experiencing negative returns.

The Custom Infrastructure, Utilities and A-REITs Accumulation Index returned -9.39% during the quarter, taking its 12-month return to -13.55%. In comparison, the broader S&P/ASX 300 Index returned 0.45% for the quarter and, globally, the MSCI World Index returned -15.70%.

### Portfolio review

#### Key Contributors

**Chorus (CNU, overweight)** – the regulated utility outperformed during the period following another upgrade to its distribution guidance at its August result and the announcement of a buyback. Operationally the business is performing well with 30% of new plans now at the unregulated pricing speed 1Gbps

or higher (vs 23% of the back book). 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 FY24 dividend yield of 6% into the medium term.

**APA Group (APA, underweight)** – the gas pipeline operator underperformed in the period in which it announced its CEO would be departing, formally stepped away from its North American strategy and an inline result. 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 do not see its valuation (at a 12-month EV/EBITDA of 13.5 times) as sufficiently compelling when compared to large cap infrastructure alternatives.

**Port of Napier (NPH, overweight)** – the port operator outperformed during the quarter in which it gave a quarterly update demonstrating steady improvement across the business as operating conditions normalise and reiterated guidance. The improvement in global supply chains and shipping reliability is positive for NPH and the resumption of cruise line activity, although likely below pre covid levels, will add high incremental margin revenues.

### **Key Detractors**

**Charter Hall Group (CHC, underweight)** – the fund manager REIT outperformed over the period, reversing prior periods of underperformance as growth related REITs suffered amid concerns around higher real yields and the prospect for lower FUM growth as the commercial real estate valuation cycle moderates. CHC's FY2022 result in August revealed a strong start to the FY2023 year from a transaction perspective, supporting the stock price. However, we remain underweight the stock based on our view that AUM growth and transaction volumes – which are running at elevated levels relative to history – will normalise in the longer term as the cap rate compression cycle reverses. As the growth rate of the business slows from impressive double-digit levels, we expect pressure on the earnings multiple, constraining share price performance. Within the real estate fund manager space, our preference is with Goodman Group (GMG).

**Scentre Group (SCG, underweight)** – our underweight position in the property REIT detracted over the period as the stock firmed following the release of its first half accounts. The strong rebound reflects ongoing improvement in operating metrics (visitations, occupancy), high levels of CPI linkages in specialty leases and robust underlying asset valuations. Despite the stock trading at 0.73 times NTA and offering a 6.0% dividend yield, we see superior risk adjusted returns in peer retail owners such as Vicinity Centres (VCX) and Bunnings Trust (BWP).

**National Storage (NSR, underweight)** – the underweight position in the storage asset owning REIT NSR detracted value as the stock performed well following release of its FY2022 financials in-line with market consensus, but guiding FY2023 underlying earnings EPS ahead of expectations (11.1cps versus consensus of 10cps). The result demonstrated strong group occupancy (88.9% vs December 2021 of 87.9%) and management see scope to grow this to 92%, providing leverage from the relatively high fixed cost base. Cap rates across the portfolio also continued to firm supporting the asset backing appeal of the stock. At current levels we remain underweight due to consumer headwinds into 2023, coupled with an unappealing stock valuation (4.6% dividend yield, 1.0 times NTA).

### **Key Purchases**

**Dexus Property (DXS)** – the portfolio has waited patiently for an opportunity to buy DXS, which presented over the period as office-market concerns excessively hit the DXS share price, to present now upside risk, in our view. Quality bifurcation is the key insight we carry when forecasting the outlook for DXS. While the fundamentals have weakened at a market level for

Sydney and Melbourne office markets (71% of DXS' office assets) our research suggests their portfolio will outperform owing to the higher exposure to prime buildings (94% by value) with strong ESG credentials, leading to superior occupancy and rental outcomes. Finally, stock valuation is now attractive, with the stock trading at 0.66 times NTA, which is excessive, in our view.

**Centuria Industrial REIT (CIP)** – we added CIP to the portfolio following the release of the passive trust's FY2022 accounts and evaluation of the compelling risk-adjusted return the shares offer currently. We believe expectations of asset value decline have gone too far for the Trust (last cap rate 4.19%) given its high-quality nature (average lease tenure 8+ years, capital city asset locations) and attractive rental outlook supported by observed re-leasing spreads of +11% in the FY2022 period (49 deals). Valuation is attractive with the stock trading at 0.64 times asset backing (NTA) and offering an attractive 6.0% dividend yield.

**Origin Energy (ORG)** – we added further to the portfolios position in the energy company during the half, reducing the underweight, after it underperformed materially. ORG has a low level of Real Asset characteristics, so we would require a more compelling valuation to be overweight the company. ORG has announced the closure of its Eraring coal power plant which we view positively, given it positions the company as a capital light participant in the energy transition with a large retail customer base.

### **Key Sales**

**Atlas Arteria (ALX)** – we took the opportunity to trim the position in the toll road operator following the outperformance that resulted from IFM's approach given a material portion of the likely upside had been realised.

**Goodman Group (GMG)** – we rebalanced the position in the industrial property developer over the period to reflect our expectation of slower earnings growth for the business, driven by the implications of the cap rate cycle turning for industrial assets. We believe GMG is well placed to continue to grow earnings well above sector peers (FY2023 EPS guidance is for 11% y/y) but have recalibrated the position size given an elevated valuation at 18 times P/E 12-months forward and offering a modest 1.8% dividend yield.

**Qube Logistics (QUB)** – we trimmed the position in the port and logistics operator during the period to fund other ideas. We still maintain a position in the company, however, many of the catalysts for the stock have now played out and the anticipated slowdown in the domestic economy will temper QUB's growth outlook.

### **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 <30%) and high level of liquidity provide us with confidence that the company is appropriately positioned for the forthcoming de-valuation cycle. Lastly, GPT's valuation has become more attractive at 0.65 times trailing NTA and 6.2% dividend yield.

**Chorus (CNU)** – the quality regulated utility trades on a 6.0% 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.

**BWP Trust (BWP)** – we believe BWP trades at a compelling valuation versus peers – 1.0 times NTA (based on conservative cap rates) with a 4.8% dividend 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 has the lowest gearing levels in the sector and is set to benefit from higher inflation given CPI leases account for around 53% of its lease structures.

### Key Active Underweights

**APA Group (APA)** – we remain underweight the pipeline operator 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 12.5 times) as sufficiently compelling when compared to large cap infrastructure alternatives.

**Stockland (SGP)** – our underweight position 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, heavily supporting the first home buyer segment. Over time, SGP's valuation faces downside risk given its exposure is to second-tier shopping centres (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 impacts demand.

**SCA Property (SCP)** – our underweight position in SCG reflects longer-term concerns around the sustainability of leasing growth, leading to concerns around dividend and valuation growth sustainability. While industry evidence of retail valuations largely held through the June-22 reporting period (VCX and SCP declare cap rate tightening into June-22) we see this as temporary only and expect valuation declines in future periods. Additionally, SCG's relatively high level of debt and lower hedged position leaves it vulnerable compared to large cap retail peers, such as Vicinity Group. With the stock trading at 0.73 times NTA and offering a 6.0% dividend yield, we see superior risk adjusted returns in peer retail owners such as Vicinity Centres (VCX) and Bunnings Trust (BWP).

### 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 and exposure to recovering economies, qualities both present within the transportation infrastructure sector. Tollroads are at the forefront of the post COVID-19 recovery and at Atlas Arteria (ALX) we see several catalysts on the horizon and are not surprised to see recent corporate interest in the name. Chorus is a quality regulated utility trading on a 5.85% FY23 dividend yield with medium term upside in regulatory returns. 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 slow and even decrease capital values (i.e. REIT NTA's) as investor acquisition return requirements 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 3 years).

## Top 5 holdings

	Portfolio	Benchmark	Active
Transurban	19.31	19.23	0.08
Goodman	13.28	13.61	-0.33
GPT	7.98	3.72	4.26
Dexus	5.91	4.21	1.70
Vicinity Centres	5.62	3.41	2.22

## Key active positions

Overweights	Portfolio	Benchmark	Active
GPT	7.98	3.72	4.26
Chorus	4.45	1.49	2.96
BWP Trust	3.46	0.90	2.55
Underweights			
APA	0.00	5.74	-5.74
Stockland	0.00	3.96	-3.96
Scentre	3.32	6.69	-3.37

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>37.52</b>	<b>31.22</b>	<b>6.30</b>
Airport Services	0.00	0.70	-0.70
Highways & Railtracks	23.95	23.08	0.87
Communication Services	5.62	1.73	3.89
Railroads	0.00	3.22	-3.22
Marine Ports & Services	5.59	2.49	3.10
Information Technology	2.36	0.00	2.36
<b>Utilities</b>	<b>3.22</b>	<b>12.34</b>	<b>-9.12</b>
Electric Utilities	3.22	4.52	-1.30
Gas Utilities	0.00	5.74	-5.74
Multi-Utilities	0.00	2.08	-2.08
<b>Real Estate Investment Trusts (REITs)</b>	<b>55.68</b>	<b>56.44</b>	<b>-0.76</b>
Specialized REITs	5.74	3.91	1.83
Diversified REITs	13.02	17.16	-4.14
Industrial REITs	15.02	14.57	0.44
Office REITs	5.91	5.22	0.70
Retail REITs	14.23	14.89	-0.66
Other	1.76	0.69	1.07
<b>Cash and receivables</b>	<b>3.58</b>	<b>0.00</b>	<b>3.58</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\$14.9 mn as at 30 September 2022	
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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