

Yarra Ex-20 Australian Equities Fund

Gross returns as at 31 December 2021

	From 25 July 2018 ^A	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception % p.a.*
Yarra Ex-20 Australian Equities Fund	6.18	2.16	2.81	17.57	12.69	8.02	10.14	8.28
S&P/ASX 300 ex S&P/ASX 20 Accumulation Index [#]	9.32	2.54	3.26	17.85	15.27	NA	NA	NA
Excess return (before fees) [‡]	-3.14	-0.37	-0.45	-0.28	-2.58	NA	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 December 2021

	From 25 July 2018 ^A	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception % p.a.*
Yarra Ex-20 Australian Equities Fund	5.21	2.08	2.58	16.52	11.67	6.91	8.87	7.02
S&P/ASX 300 ex S&P/ASX 20 Accumulation Index [#]	9.32	2.54	3.26	17.85	15.27	NA	NA	NA
Excess return (after fees) [‡]	-4.11	-0.45	-0.68	-1.33	-3.60	NA	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 prepared on an exit to exit basis – they include all ongoing fees and expenses and assume reinvestment of all distributions.

^A Effective 25 July 2018 the Fund's investment strategy, name and benchmark was changed. Performance prior to 25 July 2018 is provided here for consistency purposes only – the historical performance data shown relates to the previous strategy and should not be used to assess past or future performance of the Fund. See [here](#) for further information. Performance data relating to the previous strategy is available upon request. 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 Yarra Ex-20 Australian Equities Fund: August 2010.

[#] The benchmark for the Yarra Ex-20 Australian Equities Fund has been amended since the Fund's inception. Effective 25 July 2018, the benchmark is the S&P/ASX 300 ex S&P/ASX 20 Accumulation Index, replacing the S&P/ASX 300 Accumulation Index.

[‡] Excess return: The difference between the Fund's return and the benchmark return.

Market review

Australian equities rose modestly in the December 2021 quarter as strong performances from the miners and defensive sectors offset weakness elsewhere.

The ASX 300 Ex-20 Accumulation Index rose 3.3% during the quarter, outperforming the broader ASX300's 2.2% return and taking its 12-month return to 17.8%. The local index underperformed global indices, with the MSCI World Index returning 8.2% during the quarter even as a new COVID variant, labelled Omicron, drove uncertainty around the growth outlook. Further, persistent inflation in the US continued to stoke concerns about faster tapering and US interest rate rises.

At a sector level, Metals & Mining (+19.3%) provided the most support to the benchmark as commodity prices continued to rise. Battery materials producers Lynas Rare Earths (LYC, +51.6%), Mineral Resources (MIN, +25.0%), Pilbara Minerals (PLS, +56.1%) and IGO Limited (IGO, +29.2%) were among the top performers.

Other strong performing sectors were Real Estate (+5.1%) and Transportation Infrastructure (+3.3%). The former was supported by fund manager REIT Charter Hall Group (CHC +21.1%) and widespread gains from Retail REITs (+5.4%), while the latter saw gains from Sydney Airport (SYD, +5.3%) and Atlas Arteria (ALX, +6.6%).

Conversely, Energy (-7.2%) and Financials (-5.8%) were the worst performing sectors. The former was weighed down by the oil price which declined late in the period. The latter saw losses across the regional banks (-11.1%) and Insurance (-6.4%).

Portfolio review

Key Contributors

Link Administration (LNK, overweight) – the share registry company outperformed after receiving several takeover offers during the period and giving a positive trading update. The highest offer came from Canadian-based group Dye & Durham at \$5.50 per share, representing a 28% premium to its closing

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price prior to an earlier offer from Carlyle Group. The LNK board has recommended shareholders vote in favour of the scheme in the absence of a superior proposal. LNK also gave a trading update during the period, reaffirming full-year guidance and commenting that year-to-date trading has been ahead of expectations. We remain overweight as the corporate activity supported our view of the latent value in the business. We hold a positive view of PEXA premised on the infrastructure-like characteristics of the property settlement exchange upon maturity, supplemented by numerous growth opportunities in immediate adjacencies. Further, LNK is positively leveraged to higher US interest rates, which we see as a meaningful tailwind over the medium term.

IGO Limited (IGO, overweight) – the battery materials producer outperformed alongside the lithium price. We remain overweight the company. Our positive thesis is premised on its US\$1.4bn Greenbushes acquisition and its existing portfolio of high-quality assets. We support the acquisition for several reasons. Not only does it give IGO exposure to a high-quality, long-dated asset (>20 years mine life), but it also completes IGO's suite of battery commodities with the company already producing nickel, copper and cobalt. We also think the purchase price was reasonable, with Greenbushes likely to be NPV and EPS accretive earlier than FY23. We also hold a positive view of IGO's Nova asset – a world-class reserve which supports an increasing production profile.

Incitec Pivot (IPL, overweight) – the company outperformed after delivering a better-than-expected FY21 result and as ammonia prices moved to record highs. Management reported underlying NPAT of \$359mn, well above consensus for \$297mn, with strong performances from both the fertiliser and explosives divisions. Meanwhile, the December Tampa ammonia price increased by 20% to US\$990/t, with margins increasing as US gas prices remained relatively low. We remain overweight the company. While we are likely near the top of the cycle for fertiliser prices, we believe this is mostly reflected in consensus expectations. However, persisting spot prices would result in significant earnings upgrades and potential capital management initiatives, particularly if IPL can maintain its improved plant performance (running at nameplate capacity).

Key Detractors

TPG Telecom (TPG, overweight) – the telecommunication services company partially retraced outperformance from prior months as its founder sold a block of shares during the period. Our positive view is premised on the improving outlook for the mobiles market, recovery in volumes post COVID and the recently completed Vodafone merger, which in our view will unlock significant synergies. The combined entity is well placed to harness its infrastructure, scale and balance sheet to disrupt incumbents Telstra (TLS) and Optus through its lower-cost structure, as well as new products such as Fixed Wireless.

Star Entertainment (SGR, overweight) – the casino operator underperformed in response to media allegations that it had enabled suspected money laundering, fraud and foreign interference. Following the allegations, the company

announced that the Liquor and Gaming Authority's regular review of The Star Sydney would now also incorporate public hearings. We exited our position following extensive engagement with management and after undertaking independent validation in relation to media allegations that the company enabled suspected money laundering, fraud and foreign interference. We had taken some comfort from SGR having undergone several recent reviews without any major issues identified, in stark contrast to Crown Resorts (CWN). However, the allegations raise the risk profile of the stock, introduces the possibility there may be sanctions against the company, and may remove potential upside opportunities (extra gaming licences, concessions).

Alumina (AWC, overweight) – the alumina producer partially retraced prior outperformance without any materially negative news during the period. We remain overweight the company. We expect global aluminium demand to continue to improve as the Transportation sector recovers and, more broadly, the drive to decarbonise increases demand for the lightweight metal. More broadly we continue to hold a positive view of AWC's high-quality assets and strong earnings, cash flow and capital management potential. As a result, we see its valuation (at a forward P/E of 10.6 times with a 9.3% forecast dividend yield) as attractive.

Key Purchases

Insurance Australia Group (IAG) – we established a position in the insurer during the period for several reasons. We took advantage of recent underperformance, which reflected IAG enduring an unusually high level of mid-sized events FYTD (at ~8 times normal losses). As a result, the stock was trading at a 20% discount to the ASX 200 on FY23 earnings, well below its long-run average of -2%. While we acknowledge the structural pressure on catastrophe allowances and that IAG will need to increase its loss estimates going forward, we believe this is mostly captured by consensus. Further, IAG has \$1.15bn of business interruption reserves, most of which we believe will not be required – putting the company in a strong capital position. With \$12.5bn in policyholder and shareholder funds, IAG also has significant positive interest rate leverage: every 10 bp increase in base rates translates to a 1% increase in NPAT.

Amcor (AMC) – we established a position in the packaging company late in the quarter. We view AMC as a defensive stock with a strong dividend yield (+4.2%) that should generate strong EPS growth in FY22 (+13%), before returning to more normal levels from FY23 onwards (mid-single digit). While AMC's Flexibles division faces volume headwinds as customers turn away from non-recyclable plastics, we believe the company is moving in the right direction from the point of view of producing more recycled product, and using more post-consume resin. Further, shifts to higher margin customers (pharmaceutical and medical) and cost-out initiatives will provide an offset. Lastly, we view AMC's valuation as attractive at 13.8 times forward P/E, below its 15.4 times long-term average.

Link Administration (LNK) – we increased our position in the company during the period, prior to the company agreeing to a takeover offer from Canadian-based Dye & Durham. We see compelling value in its base share registry business and electronic conveyancing business PEXA, which has been supported by recent corporate interest. We hold a positive view of PEXA premised on its infrastructure-like characteristics of the property settlement exchange upon maturity, supplemented by numerous growth opportunities in immediate adjacencies. Further, LNK is positively leveraged to higher US interest rates, which we see as a meaningful tailwind over the medium term. Lastly, LNK trades at 24.2 times forward earnings, a discount to peer Computershare (CPU) at 24.9 times.

Key Sales

Iluka Resources (ILU) – we exited our position during the period. We are cautious about the company's operating outlook as developments in China's real estate industry slows from elevated levels, which we believe is not fully reflected despite its headline valuation multiple (forward EV/EBITDA of 4.7 times). We regard the industry structure as attractive (consolidated supply), with less pricing volatility compared to previous cycles. Our preferred mining exposures at this time include BHP Group (BHP), IGO Limited (IGO) and Alumina (AWC).

Star Entertainment (SGR) – we exited our position following extensive engagement with management and after undertaking independent validation in relation to media allegations that the company enabled suspected money laundering, fraud and foreign interference. We had taken some comfort from SGR having undergone several recent reviews without any major issues identified, in stark contrast to Crown Resorts (CWN). However, the allegations raise the risk profile of the stock, introduces the possibility there may be sanctions against the company, and may remove potential upside opportunities (extra gaming licences, concessions).

Lendlease (LLC) – we exited our position in the property group during the period in response to greater uncertainty over the outlook and to fund more compelling, near-term opportunities elsewhere. LLC's strategy targets have been pushed out to FY24 (from FY23/24 previously) as COVID continues to impact LLC's real estate markets, particularly its UK developments, and the new chief executive reset earnings expectations with a more conservative approach to profit recognition.

Key Active Overweights

Link Administration (LNK) – we are positive on the company because we see compelling value in its base share registry business and electronic conveyancing business PEXA, which has been supported by recent corporate interest with the board agreeing to a \$5.50 per share near period-end by Canadian-based Dye & Durham. We hold a positive view of PEXA premised on its infrastructure-like characteristics of the property settlement exchange upon maturity, supplemented by numerous growth opportunities in immediate adjacencies. Further, LNK is positively leveraged to higher US interest rates, which we see as a meaningful tailwind over the medium term.

Lastly, LNK trades at 24.2 times forward earnings, a discount to peer Computershare (CPU) at 24.9 times.

Atlas Arteria (ALX) – we maintain a high-conviction overweight position based on ALX's strong liquidity and balance sheet position, discounted valuation and exposure to traffic recovery in Europe and the US. ALX on less than 11.0 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. Beyond traffic normalisation, we see a path towards value creation for ALX through concession extensions at APRR achieved as a means of funding expansion projects and settling the Dulles Greenway tolling regime.

James Hardie (JHX) – we continue to believe JHX is well positioned to benefit from the stronger US housing environment following the resolution of the COVID-19 crisis. JHX has the ability to sustain growth ahead of the market and sell higher value products, which will more than compensate for risks around growth rates normalising and higher borrowing costs. We are confident in the company's market share outlook due to its high-quality and reliable products, improved sales strategies (positioning the product as superior versus alternatives) and the resolution of US supply and manufacturing issues. We view JHX's valuation as attractive at 25.3 times forward earnings, below the Industrial ex-Financials at 28.6 times despite the stock's superior growth outlook.

Key Active Underweights

Sydney Airport (SYD) – we are underweight on the grounds that the latest takeover offer for the company fully reflects its recovery at \$8.75 per share and, at an EV of 23 times CY19 earnings, is above other major airport transactions globally. Further, if it is unsuccessful, there are 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 2022 which, if they are not extended, may result in adverse pricing outcomes for the airport operator.

Sonic Healthcare (SHL) – we are underweight the company on the grounds positive vaccine outcomes are likely to create an earnings headwind for the company which has seen significant earnings support from its COVID-19 testing services. While short-term earnings will remain robust, we expect EBITDA to decline in FY23 as fewer tests are issued. We no longer view its valuation as sufficiently compelling versus alternatives, with the company trading 19.6 times elevated forward earnings.

Santos (STO) – we remain positive towards the company on a fundamental basis, premised on its resilient low-cost base business (break-even <US\$25/bbl); a diversified asset base across multiple basins, customers and products (with 60% oil exposure); latent value in its midstream infrastructure and a defined pathway to net zero emissions. However, we note emissions cuts rely heavily on scaling carbon capture and storage (CCS) and hydrogen – two unproven technologies at scale – without committing significant capital to shifting the business to a low carbon world. We view the proposed merger

with Oil Search (OSH) as logical from a financial perspective, however at this stage it is unclear how the merger affects the group's climate change strategy.

Market outlook

We expect the Australian economy to continue to rebound in the short-term, following a better-than-expected contraction in 1Q21 amid COVID-related lockdowns in Melbourne and Sydney.

Notwithstanding the ongoing risk from new variants such as Omicron, we believe any interruption to economic growth from renewed lockdowns will be an aberration within an improving trend. Indeed, the fundamentals that will drive the economic recovery remain in place. The recovery in labour market income has been sufficient to offset the gradual withdrawal of temporary fiscal support. Moreover, the accumulation of an estimated \$185bn in excess household saving, in concert with strong asset price gains, leaves the consumer uniquely positioned to underpin economic growth in 2021-2022. Dwelling investment is set to provide solid support for economic growth over the next six months as previously approved housing moves through the construction phase, and a broader-based lift in business investment expectations is an important step in ensuring a sustained economic recovery. We expect the global economy to have expanded 6% in 2021 and the Australian economy 4.5%. We expect another strong year of economic growth in 2022 of 4.0%.

Nevertheless, there are some areas that are cause for concern. For over 12 months we have warned about rising US inflation pressures and rising inflation expectations. However, supply chain constraints and energy shortages in the Northern Hemisphere risk inflation pressures becoming more widespread and more entrenched. With the peak in global business surveys having passed, cost inflation continuing to escalate and the Federal Reserve announcing its decision to taper its bond purchases, we expect bond yields will move higher, providing some ongoing challenges for risk assets.

The A\$/US\$ has recently been buffeted by concerns of a peak in global industrial growth indicators, slowing China economic momentum and recent declines in iron ore prices. Nevertheless, Australia's external accounts are in their best position since the early 1970s and despite some moderation in commodity prices we expect the A\$/US\$ to remain supported by global reflationary forces through 2022.

We are most overweight stocks within the Telecommunication Services, Media & Entertainment and Materials sectors, and are underweight Real Estate, Health Care and Industrials.

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	13.78	4.71	9.07
Consumer Discretionary	4.97	8.54	-3.57
Consumer Staples	2.33	3.99	-1.66
Energy	3.45	5.05	-1.60
Financials	13.61	12.96	0.64
Health Care	6.45	9.21	-2.77
Industrials	7.84	10.39	-2.55
Information Technology	10.64	8.06	2.58
Materials	25.93	21.38	4.55
Real Estate	3.97	12.67	-8.70
Utilities	3.62	3.04	0.58

Top 5 holdings

	Portfolio %	Benchmark %	Active %
James Hardie Industries	6.44	2.49	3.96
QBE Insurance	5.47	1.69	3.78
Link Administration	5.18	0.29	4.89
Atlas Arteria	4.83	0.67	4.16
Northern Star Resources	4.41	1.11	3.31

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
Link Administration	5.18	0.29	4.89
Atlas Arteria	4.83	0.67	4.16
James Hardie Industries	6.44	2.49	3.96
Underweights			
Sydney Airport	0.00	2.37	-2.37
Sonic Healthcare	0.00	2.26	-2.26
Santos	0.00	1.94	-1.94

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.

Income and growth

	1 year %	3 years % p.a.	5 years % p.a.	Since inception % p.a.
Growth return	14.39	9.45	4.39	4.27
Distribution return	2.13	2.22	2.52	2.75

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 capital distributions.

Features

Investment objective	To achieve medium-to-long term capital growth through exposure to Australian Securities Exchange listed securities excluding the largest 20 by market capitalisation (as defined by the S&P/ASX 20 Index). In doing so, the aim is to outperform the S&P/ASX 300 ex S&P/ASX 20 Accumulation Index over rolling 3-year periods.	
Recommended investment time frame	5 - 7 + years	
Fund inception	August 2010	
Fund size	A\$14.1 mn as at 31 December 2021	
APIR code	JBW0052AU	
Estimated management cost	0.90% p.a	
Buy/sell spread	+/- 0.15%	
Platform availability	BT Panorama Hub24	Praemium

Applications and contacts

Investment into the Yarra Ex-20 Australian Equities Fund can be made by Australian resident investors only.

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