

Yarra Ex-20 Australian Equities Fund

Gross returns as at 31 January 2022

	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	4.35	-5.60	-3.36	12.66	8.90	7.17	8.99	7.68
S&P/ASX 300 ex S&P/ASX 20 Accumulation Index [#]	6.64	-7.88	-5.04	9.97	10.13	NA	NA	NA
Excess return (before fees) [‡]	-2.29	2.28	1.68	2.70	-1.22	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 January 2022

	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	3.40	-5.67	-3.58	11.66	7.92	6.08	7.74	6.42
S&P/ASX 300 ex S&P/ASX 20 Accumulation Index [#]	6.64	-7.88	-5.04	9.97	10.13	NA	NA	NA
Excess return (after fees) [‡]	-3.24	2.21	1.46	1.69	-2.21	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 declined sharply in January as high inflation spurred Federal Banks to accelerate quantitative tapering and signal earlier rate rises.

The ASX 300 Ex-20 Accumulation Index declined 7.9% during the month, underperforming the broader ASX300's -6.5% return and taking its 12-month return to 10.0%. Globally, the S&P500 and MSCI World Index returned -5.2% and -4.9% respectively as US real yields rose, with the US 10-year Treasury Inflation-Protected Securities (TIPS) climbing 38 bps to -0.69% as the US Fed said it would likely start to increase interest rates in March.

At a sector level, high-P/E cohorts within Health Care (-14.7%) and Information Technology (-14.5%) recorded the most significant declines, led by companies with long-dated cash flows like Xero (XRO, -20.2%), Wisetech Global (WTC, -22.7%), Altium (-21.0%) and Pro Medicus (PME, -27.8%). Gold (-13.2%) also declined significantly given its negative correlation with real interest rates.

Conversely, Energy (+4.6%) was the strongest performer as Brent Crude lifted by 18% to US\$92/bbl. Oil & Gas producers Santos (STO, +13.2%), Beach Energy (BPT, +17.5%) and engineering services company Worley (WOR, +8.7%) were among the top performers. Utilities (+2.6%) also increased in value during the period amid the outlook for higher electricity prices, supported by AGL Energy (AGL, +15.6%) and Origin Energy (ORG, +7.3%).

Portfolio review

Key Contributors

Worley (WOR, overweight) – the engineering services company outperformed as oil prices increased, with Brent Crude rising 18% to US\$92/bbl during the period. We remain overweight WOR, which we believe is in a strong position to withstand a lower-than-expected recovery in its traditional work. Following the Jacobs ECR acquisition, the business is diversified across different markets and is well positioned to capture higher structural demand from energy transition work to low carbon solutions. We believe WOR's valuation provides

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significant support at current levels, with the stock trading on 16.5 times forward earnings, a sharp discount to the Industrials ex-Financials at 24.7 times.

Origin Energy (ORG, overweight) – the energy company outperformed as oil prices increased – with Brent Crude rising 18% to US\$92/bbl during the period – 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 overweight the company. At current valuation levels (15.2 times forward earnings), the market factors in ORG's energy transition risks but largely ignores potential upside as the company improves its emissions profile. Following the closure of Eraring, ORG's emissions intensity will be half that of the national electricity market, with no coal exposure and a credible pathway to decarbonise further through increased renewables penetration.

TPG Telecom (TPG, overweight) – the telco held its value during the period without any material news, outperforming the declining market. Our thesis 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.

Key Detractors

Santos (STO, underweight) – the oil & gas producer outperformed as oil prices increased – with Brent Crude rising 18% to US\$92/bbl during the period – and in response to a strong 4QFY22 result. While production of 22.9mmbob and sales volumes of 26mmbob were in line with expectations, the company delivered record revenue as realised LNG prices increased by 32% to US\$13.64/mmbtu. We remain positive towards the company on a fundamental basis, premised on its resilient low-cost base business, a diversified asset base across multiple basins, customers and products (with 60% oil exposure) and latent value in its midstream infrastructure. However, we note its emissions reduction strategy relies 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 recently completed 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.

James Hardie (JHX, overweight) – the building materials company partially retracted strong outperformance from prior periods following the announcement that its chief executive had been dismissed, effective immediately, due to conduct breaches. The announcement overshadowed an upgrade to FY22 guidance, with NPAT now expected to be US\$615mn at the midpoint compared to US\$590 previously. We reduced our holdings to reflect the increased uncertainty and capture earlier outperformance. We continue to believe JHX can

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.

Ansell (ANN, overweight) – the protective equipment manufacturer outperformed after downgrading FY22 earnings guidance during the period. Management cut EPS guidance by 22% to \$1.35 per share, citing a slowdown in Exam and the single-use market, the US Customs and Border Protection (CBP) agency placing a ban on one of its key medical glove suppliers and, lastly, Omicron causing a manufacturing outage at its facility. We remain overweight the company on the grounds that earnings risks are now largely reflected in its share price. ANN trades at 13.9 times forward consensus earnings, a sharp discount to the wider Industrials ex-Financials at 24.7 times.

Key Purchases

Amcor (AMC) – we increased our position in the packaging company during the period. We view AMC as a defensive stock with a strong dividend yield (+4.0%) 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 14.9 times forward P/E, below its 15.4 times long-term average.

Key Sales

James Hardie (JHX) – we reduced our holdings to reflect the increased uncertainty associated with the chief executive's dismissal from the company and to capture earlier outperformance. However, we maintain a smaller overweight position. We continue to believe 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.

Mirvac Group (MGR) – we reduced our position due to increased uncertainty on the sustainability of development profits. We are cautious towards the housing outlook as approvals retreat from elevated levels, which will impact MGR's residential division. Further, we see risk to development profits on the non-commercial side with the prospect cap rates rise. That being said, we maintain a small overweight position in the company on the grounds these risks are largely reflected

in consensus forecasts, with the stock trading at 0.8 times trailing NTA.

Origin Energy (ORG) – we reduced our position following recent outperformance but remain overweight the energy company. At current valuation levels (15.2 times forward earnings), the market factors in ORG's energy transition risks but largely ignores potential upside as the company improves its emissions profile. Following the closure of Eraring, ORG's emissions intensity will be half that of the national electricity market, with no coal exposure and a credible pathway to decarbonise further through increased renewables penetration.

Key Active Overweights

Link Group (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. 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 23.2 times forward earnings, a discount to the Industrials ex-Financials at 24.7 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.

TPG Telecom (TPG) – 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.

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.

Santos (STO) – we remain positive towards the company on a fundamental basis, premised on its resilient low-cost base business, a diversified asset base across multiple basins, customers and products (with 60% oil exposure) and latent value in its midstream infrastructure. However, we note its emissions reduction strategy relies 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 recently completed 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.

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 16.3 times elevated forward earnings.

Market outlook

The pattern of quarterly economic growth in Australia remains volatile, having declined 1.7% (q/q) in 3Q under the impact of the Delta strain of COVID. Nevertheless, record fiscal stimulus and easy financial conditions have helped underpin solid real economic growth of 3.9% (y/y) and a 4Q recovery from the Delta variant disruption is expected to see real economic growth in calendar 2021 to average 4.0%.

Recovering underlying household income growth, \$200bn in 'excess saving', strong corporate profit growth, low inventory levels and robust capex expectations – in concert with a still solid global growth backdrop – suggests Australian economic growth into 2022 will be above 'potential'. In both CY2022 and CY2023 we expect the Australian economy to expand at an above 'potential' rate of 3%.

The strength of the economic recovery has been particularly evident via the strength in employment. After peaking at 7.5% in July 2020, the unemployment rate has declined sharply to 4.2% in December 2021. In essence the unemployment rate is now in line with the RBA estimate of non-accelerating inflation rate of unemployment (NAIRU) and the combination of excess demand relative to available supply has seen 2H21 produce sufficient broad based inflation pressures to prompt an abrupt reassessment of the RBA's monetary stance. We expect the RBA will commence increasing interest rates in 4Q2022 with a 35 bps hike, with a further four 25 bps rate hikes in 2023.

Although we remain constructive on global economic growth, we believe the industrial cycle peaked in mid-2022 and that a relatively controlled slowing in economic activity is currently taking place. Nevertheless, there are some areas that are cause for concern. For over 18 months we have warned about rising US inflation pressures and rising inflation expectations, and while these threats have been realised, 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 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 volatility in commodity prices. Nevertheless, Australia's external accounts are in their best position since the early 1970s and despite some moderation in commodity prices the A\$/US\$ should remain supported by the RBA joining other central banks in tightening interest rates this year. We expect the A\$ will finish CY 2022 at around 76 cents.

We are most overweight stocks within the Communication Services, Materials and Information Technology sectors, and are underweight Real Estate, Consumer Discretionary and Industrials.

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	13.49	4.61	8.88
Consumer Discretionary	4.93	8.50	-3.57
Consumer Staples	2.17	3.91	-1.73
Energy	3.99	5.74	-1.75
Financials	14.26	13.10	1.16
Health Care	5.98	8.53	-2.55
Industrials	7.88	10.54	-2.66
Information Technology	10.27	7.48	2.79
Materials	24.77	21.59	3.19
Real Estate	2.90	12.60	-9.71
Utilities	3.68	3.38	0.30

Top 5 holdings

	Portfolio %	Benchmark %	Active %
QBE Insurance	5.71	1.80	3.90
Link Administration	5.32	0.30	5.02
Atlas Arteria	4.83	0.69	4.14
TPG Telecom	4.20	0.24	3.96
Northern Star Resources	4.14	1.06	3.08

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
Link Administration	5.32	0.30	5.02
Atlas Arteria	4.83	0.69	4.14
TPG Telecom	4.20	0.24	3.96
Underweights			
Sydney Airport	0.00	2.56	-2.56
Santos	0.00	2.39	-2.39
Sonic Healthcare	0.00	2.00	-2.00

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.	10 years % p.a.
Growth return	9.61	5.77	3.58	4.92
Distribution return	2.04	2.14	2.50	2.81

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\$13.1 mn as at 31 January 2022	
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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