

Yarra Ex-20 Australian Equities Fund

Gross returns as at 31 October 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	5.76	0.43	4.30	24.78	8.16	8.71	9.30	8.18
S&P/ASX 300 ex S&P/ASX 20 Accumulation Index [#]	8.82	0.18	4.08	26.00	12.41	NA	NA	NA
Excess return (before fees) [‡]	-3.06	0.26	0.22	-1.23	-4.25	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 October 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	4.79	0.36	4.06	23.67	7.18	7.58	8.03	6.92
S&P/ASX 300 ex S&P/ASX 20 Accumulation Index [#]	8.82	0.18	4.08	26.00	12.41	NA	NA	NA
Excess return (after fees) [‡]	-4.03	0.18	-0.02	-2.34	-5.23	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 were flat in October, underperforming global equities as Australian bond yields rose sharply in response to higher inflation expectations.

The ASX 300 Ex-20 Accumulation Index lifted 0.2% during the month, taking its 12-month return to 26.0%. The local index underperformed global indices – with the MSCI World Index returning 5.5% – as Australian 10-year bond yields lifted 59 bps to 2.08% during the period on expectations the RBA would hike rates earlier amid inflation pressure.

Gold (+9.7%) was the top performer during the period, with the sector seen as a beneficiary of stronger inflation. At a stock level, Northern Star (NST, +8.7%), Silver Lake Resources (SLR, +26.5%) and West African Resources (WAF, +34.0%).

Information Technology (+2.8%) also delivered a solid return, with the sector supported by lower real yields. The best performing stocks included Xero (XRO, +7.6%), Appen (APX, +20.0%) and Nearnmap (NEA, +16.6%).

Conversely, Banking (-4.3%) and Insurance (-3.7%) were among the worst performers. Bank of Queensland (BOQ, -3.7%) and Bendigo & Adelaide Bank (BEN, -2.1%) weighed on the benchmark, with the former guiding to higher costs in its FY21 result. Meanwhile, Suncorp (SUN, -6.7%) announced higher-than-expected claims for the first four months of FY22 as a result of several storm events during the period.

Portfolio review

Key Contributors

Northern Star (NST, overweight) – the gold miner outperformed during the period alongside the gold price (+2% to \$US1,784) and as the gold sector was seen as a beneficiary of higher inflation. The macro-environment outweighed NST's slightly softer-than-expected 1Q21 result. Production came in at 373,000 ounces, 6% below consensus forecasts, while costs were 5% above at \$1,594 per ounce. We remain overweight NST. We believe the company will benefit from higher-than-expected production and reserves/resources after taking full ownership of the KCGM SuperPit Mine in February

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this year. We see the company's valuation as attractive at 5.8 times forward EV/EBITDA, which is only marginally above the wider Gold sector's 5.4 times despite a superior growth outlook. More broadly, we have a neutral exposure to the commodity, balancing the prospect of higher inflation with an uncertain rate hike path in the US (which is generally a headwind to the gold price).

Worley (WOR, overweight) – the engineering services firm outperformed during the period after winning several new contracts which highlighted its position as an energy transition beneficiary. In particular, it won a contract from Shell to help develop a facility in the Netherlands that will produce sustainable aviation fuel (SAF) and renewable diesel from waste. We remain overweight the company, 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 significant support at current levels, with the stock trading on 15.4 times forward earnings, a sharp discount to the Industrials ex-Financials at 29.4 times.

JB Hi-Fi (JBH, overweight) – the electronics retailer outperformed during the period after releasing a better-than-expected 1Q22 sales result. Sales fell just 6-8% y/y despite 60% of its stores being closed in NSW and Victoria due to lockdowns. We remain overweight the company. We continue to believe the market underestimates JBH's ability to grow across different trading conditions, which is not reflected in its valuation at 14.8 times 12-month forward earnings. In regards to The Good Guys, execution has improved significantly and management is now focused on maintaining the strong increase in customers as homewares benefits from the COVID-19 pandemic, which could add significant upside.

Key Detractors

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 reduced our position in the company following the media allegations. 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). We are engaging extensively with management and are undertaking further independent validation in relation to the allegations, which the company has labelled as misleading.

Ansell (ANN, overweight) – the protective equipment manufacturer underperformed during the period without any material news. We remain overweight the company. Though we expect an air pocket in exam and single-use earnings as higher capacity in the market suppresses pricing, we expect

ANN underlying earnings to reclaim its FY21 COVID peak by FY23 as underlying earnings grow. More broadly, we expect both divisions to benefit from internal programs to increase operational efficiency, higher margins from new distributor agreements and shifts towards higher-value products. Lastly, ANN has a strong balance sheet; we estimate \$220mn of buy-back capacity. We do not believe this is captured by consensus; the stock trades at 13.4 times, a large discount to the wider Industrials ex-Financials at 29.4 times.

TPG Telecom (TPG, overweight) – the telecommunication services company partially retraced outperformance from prior months without any material news 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.

Key Purchases

Link Group (LNK) – we increased our position in the company during the period. We continue to see compelling value in its base share registry business and electronic conveyancing business PEXA. Notwithstanding the PEP/Carlyle consortium walking away from its takeover proposal, we continue to see value in PEXA (with the company retaining its 45% stake in the IPO). Our positive view of PEXA is premised on infrastructure like characteristics of the property settlement exchange upon maturity supplemented by numerous growth opportunities in immediate adjacencies. Excluding PEXA, LNK trades at a forward P/E of less than 10-11 times, a substantial discount to peer Computershare (CPU) at 25.2 times.

Kathmandu (KMD) – we increased our position in the outdoor adventure retailer during the period. The company is well placed to benefit from easing travel restrictions, both domestically and internationally. Further, we see upside from its two acquisitions, Rip Curl and OBOZ, its attractive category exposure as well as market share and margin expansion opportunities. We continue to see the stock as undervalued at 14.0 times forward earnings, a sharp discount to its Specialty Retail peers at 16.1 times.

Latitude Group Holdings (LFS) – we modestly increased our position in the consumer finance company during the period. Our positive view is based on several factors. Firstly, we see its valuation as attractive at 9.1 times 12-month forward earnings, which we believe more than compensates for its small adjusted free float (28%) and selling overhang, and attractive versus peers on an average multiple of 11 times. Secondly, we see LFS as positively leveraged to the strengthening Australian consumer, both through sales and credit expenses. Lastly, we see LFS as a beneficiary of COVID-affected categories including travel services, which we don't believe is captured in market expectations.

Key Sales

Star Entertainment (SGR) – we reduced our position in the company following the media allegations that the company had 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). We are engaging extensively with management and are undertaking further independent validation in relation to the allegations, which the company has labelled as misleading.

Metcash (MTS) – we trimmed our position following recent outperformance but remain overweight the wholesale distribution and marketing company. We believe its current valuation (15.9 times forward earnings) captures the improved short-term outlook for sales and earnings trends across its businesses (supermarkets, hardware and liquor) as the company benefits from COVID-19. In our view these trends will revert over the medium term, with strong competition from Woolworths (WOW) and Coles (COL) likely to drive market share losses and negative operating leverage.

Incitec Pivot (IPL) – we trimmed our position following recent outperformance but remain overweight the fertiliser and explosives maker. We believe the risk is skewed to the upside at current levels (at 12.5 times forward earnings), particularly as operational issues are resolved. The company's key end markets – fertilisers and coal volumes – are benefiting from an emerging energy crisis globally, which we believe will result in upgrades to consensus forecasts. As an ammonia producer in the US, IPL is benefiting from a widening spread between Ammonia prices (where the marginal producer is in Europe) and the US natural gas price.

Key Active Overweights

Link Group (LNK) – we are overweight the company because we continue to see compelling value in its base share registry business and electronic conveyancing business PEXA. Notwithstanding the PEP/Carlyle consortium walking away from its takeover proposal, we continue to see value in PEXA (with the company retaining its 45% stake in the IPO). Our positive view of PEXA is premised on infrastructure like characteristics of the property settlement exchange upon maturity supplemented by numerous growth opportunities in immediate adjacencies. Excluding PEXA, LNK trades at a forward P/E of less than 10-11 times, a substantial discount to peer Computershare (CPU) at 25.2 times.

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.

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 continues to take market share and increase margins in the key part of its business (North America comprises 70% of value), with input costs moderating from elevated levels. 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.

Key Active Underweights

Sydney Airport (SYD) – we are underweight Australia's largest airport on the grounds that the latest takeover offer for the company fully reflects its recovery at \$8.75 per share and, at 22 times FY24 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, in 2020, saw significant earnings support from its COVID-19 testing services. While short-term earnings will remain robust, we expect EBITDA to decline in FY22 as fewer tests are issued. We no longer view its valuation as sufficiently compelling versus alternatives, with the company trading 19.0 times elevated forward earnings.

Xero (XRO) – we are underweight the accounting software provider because we believe its strong growth outlook is fully factored into its valuation, but its potential risks are not. XRO trades at 18.7 times EV/sales, reflecting lofty expectations for subscriber growth to accelerate as the company continues to expand overseas and for add-on products and services to drive higher average revenue per user (ARPU). However, international expansion carries significant risks due to greater competition in more fragmented markets, with significant ongoing product reinvestment required for XRO to maintain its advantages relative to peers.

Market outlook

After completing 1H2021 with strong momentum, renewed Covid-related lockdowns in Melbourne and Sydney will see the Australian economy contract in 3Q21, albeit it has been notable how well both business surveys and employment indicators have held up in Q3, suggesting a modest contraction than might have been expected several months ago. Real-time data suggests Q4 economic growth will rebound solidly, led by the service-based industries.

We continue to believe the 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 6 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 expand 6% and the Australian economy to expand 4.5% in 2021. 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 through the remainder of 2021. We expect US 10-year yields to approach 1.80% by the end of 2021, providing some ongoing challenges for risk assets in Q4.

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 believe the A\$/US\$ should remain supported by global reflationary forces through 2021-22. We expect the A\$/US\$ to finish the year in the 76-78c range, and remain around that level through 1H22.

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

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	14.02	4.78	9.25
Consumer Discretionary	9.87	9.11	0.75
Consumer Staples	2.15	4.02	-1.88
Energy	3.45	5.09	-1.64
Financials	9.81	13.88	-4.07
Health Care	6.71	9.17	-2.46
Industrials	6.60	10.26	-3.66
Information Technology	8.85	7.99	0.86
Materials	25.69	19.87	5.83
Real Estate	5.58	12.51	-6.93
Utilities	3.56	3.31	0.25

Top 5 holdings

	Portfolio %	Benchmark %	Active %
James Hardie Industries	6.14	2.39	3.75
QBE Insurance	5.25	1.82	3.43
Northern Star Resources	4.34	1.12	3.22
Link Administration	4.12	0.24	3.88
TPG Telecom	4.11	0.26	3.85

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
Link Administration	4.12	0.24	3.88
TPG Telecom	4.11	0.26	3.85
James Hardie Industries	6.14	2.39	3.75
Underweights			
Sydney Airport	0.00	2.30	-2.30
Xero	0.00	2.01	-2.01
Sonic Healthcare	0.00	1.99	-1.99

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	21.28	4.74	4.80	4.21
Distribution return	2.39	2.44	2.78	2.71

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\$13.8 mn as at 31 October 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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Disclaimers

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