

# UBS Australian Share Fund

August 2023

## Fund description

The Fund is an actively managed fund investing in a portfolio of 30–70 listed Australian equity securities listed on the Australian Securities exchange.

## Target market

The Target Market Determination (TMD) for the Fund sets out the class of consumers for whom the product, including its key attributes, would likely be consistent with their likely objectives, financial situation and needs. To access to the TMD and other Fund documentation visit our website.

## Investment objective

The Fund aims to outperform (after management costs) the S&P/ASX 300 Accumulation Index over rolling five-year periods.

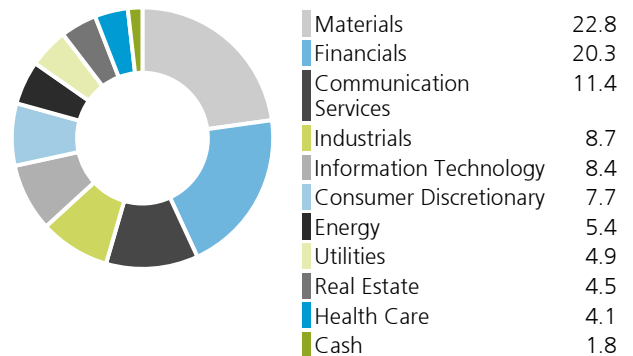
## Fund information<sup>^</sup>

|                            |               |
|----------------------------|---------------|
| Inception date             | 15 July 1992  |
| Fund size                  | \$ 229.1m     |
| Management fee*            | 0.80% pa      |
| Minimum initial investment | \$ 50,000     |
| Typical number of holdings | 30 to 70      |
| Distributions              | Semi-annually |
| Buy/sell spread            | +/- 0.25%     |
| APIR code                  | SBC0817AU     |

<sup>^</sup> The UBS Yarra Australian Share Fund has been renamed the UBS Australian Share Fund, effective as at 9 November 2022.

\* The management fees and costs for the fund have been reduced from 0.90% p.a. to 0.80% p.a effective as at 9 November 2022.

## Sector allocation (%)



## Active security positions

| Overweight                    | Underweight                     |
|-------------------------------|---------------------------------|
| Reliance Worldwide Corp. Ltd. | CSL Limited                     |
| Worley Limited                | National Australia Bank Limited |
| Origin Energy Limited         | Macquarie Group, Ltd.           |
| QBE Insurance Group Limited   | Wesfarmers Limited              |
| Carsales.Com Limited          | Woolworths Group Ltd            |

## Active industry positions

| Overweight                 | Underweight                                   |
|----------------------------|---|
| Software & Services        | Banks   |
| Capital Goods              | Pharmaceuticals Biotechnology & Life Sciences |
| Media & Entertainment      | Financial Services                            |
| Utilities                  | Consumer Staples Distribution & Retail        |
| Telecommunication Services | Commercial & Professional Services            |

## Investment performance

| Fund               | 1 month<br>%  | 3 months<br>% | 1 year<br>% | 2 years<br>% pa | 3 years<br>% pa | 5 years<br>% pa | Since inception*<br>% pa |
|--------------------|---------------|---------------|-------------|-----------------|-----------------|-----------------|--------------------------|
| Total return       | (2.61)        | 1.39          | 12.53       | 4.75            | 12.48           | 6.36            | 9.59                     |
| Benchmark**        | (0.76)        | 3.88          | 8.96        | 2.45            | 10.51           | 6.99            | 9.23                     |
| <b>Added Value</b> | <b>(1.85)</b> | <b>(2.49)</b> | <b>3.57</b> | <b>2.30</b>     | <b>1.97</b>     | <b>(0.63)</b>   | <b>0.36</b>              |

\* The UBS Asset Management price/value equities process was adopted on 1 April 1996.

\*\* S&P/ASX 300 Accumulation Index. All Ordinaries Accumulation Index prior to June 2000.

Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.

## Portfolio performance

After fees and expenses, the Portfolio decreased by 2.61% during the month, underperforming its benchmark by 184 bps.

The largest positive contributors were Carsales.com, NEXTDC and Wisetech Global. Online auto classified Carsales.com outperformed in August following its full-year FY23 results (net profit increase of 23% was higher than expectations). Similarly, NEXTDC also outperformed on the back of its FY23 results release. Our underweight position in WiseTech was a source of outperformance, as the share price of the logistics industry software solutions provider fell after reporting its full-year results (earnings guidance was lower than consensus).

The largest negative contributors were ResMed, Alumina and Wesfarmers. The medical equipment manufacturer ResMed, underperformed due to increased focus on the potential future impact of weight loss drugs, an eventual return of competitor Phillips into the sleep-apnoea device market and reported decline of its gross margin. The share price of Alumina dropped after the alumina and aluminium producer reported a net loss in their half-year report. Our underweight position in Wesfarmers was a detractor as the diversified conglomerate outperformed during the period following its solid FY23 results, which was led by the core Bunnings business and Kmart.

## Market review

Australian Equities weakened during the August month on the back of a volatile reporting season. The S&P/ASX 300 delivered a return of -0.8% for the month, taking its 12-month return to +9.0%. Similarly, the S&P/ASX 200 returned -0.7% for the period. While on the global scale, the MSCI World Index generated a return of -2.4%.

Consumer Discretionary (+5.8%) was the top performing sector, largely driven by Wesfarmers (WES, +10.6%) as shares surged after the conglomerate delivered an exceptional FY23 result and a higher dividend payout for investors.

Other positive performing sectors were Real Estate (+1.7%) and Energy (+0.7%), driven by Goodman Group (GMG, +13.7%) on the back of its FY23 results release outlining higher-than-expected operating EPS growth of 16% yoy. Within the energy sector, Ampol (ALD, +7.5%) was a strong contributor as the Australian petroleum company benefitted from a rally in the Brent oil price.

Conversely, Utilities (-3.9%) was among the weakest performing sectors with APA Group (APA, -10.1%) as the main detractor. Another stock which also underperformed was AGL Energy (AGL, -7.1%) following a statutory loss reported for FY23.

## Outlook

With the major central banks declaring that further interest rates are now data dependent and as evidence continues to accumulate that inflation continues to moderate, our long-held view that mid-2023 would mark the top of the interest rate cycle appears to be broadly on track. Crucially, both labour markets and core services inflation have eased in recent months and forward indicators suggest further progress should be made through the rest of 2023.

Moreover, the pessimistic tone of the economic activity data in the US that threatened a technical recession has given way to slightly more updated data in recent weeks encouraging the belief that the US will escape a technical recession in 2023. Indeed, some leading indicators are suggesting that a broader turn in the global industrial cycle is at hand, which should encourage a rotation from a narrow mega-cap tech led equity market rally to broader participation in 2023.

Indeed, our leading indicators suggest the negative EPS revisions trend has now largely run its course, which when combined with a levelling out in economic momentum and an end to the interest rate tightening cycle, will likely provide greater confidence in underlying valuations and a shift from bearish equity positioning. Bond yields continue to provide the more significant challenge to equity market valuations, albeit the lift in bond yields into mid-2023 can largely be attributed to a significant lift in the supply of US bonds as the US budget deficit continues to increase sharply, thereby providing a counter cyclical boost to economic growth.

Economic growth has also slowed in Australia, recording just 0.4%q/q growth in the June quarter, similar to the languid growth recorded in the March quarter. Indeed, with population growth running at a 2.5% annualised pace in the six-months to June and economic growth expanding at an annualised 1.8% pace over the same period, Australia has recorded its first per capita recession since mid-2006 (excluding the COVID lockdown period). It is clear the prior tightening of monetary policy is having a material impact on the interest rate sensitive parts of the economy. For instance, discretionary consumption volumes have declined 0.6% (six-month annualised) as non-discretionary household expenses and interest costs soared by 16%yoy – the fastest annual increase since 1989. Building approvals continue to decline – now down 45% from the 2021 peak - and are likely to fall further in coming months as declining housing affordability outweighs the impact of an under supplied housing market.

Nevertheless, the good news is that after a pause in the tightening cycle in July, The Reserve Bank of Australia (RBA) has remained on hold and flagged that future monetary policy adjustments will be data dependent. To be clear, the RBA retains a tightening bias, however an update of their inflation forecasts now has inflation returning to inside the target band in 2025, providing a signal that absent any unexpected inflation shocks the RBA's rate tightening cycle is complete. The RBA also revised down economic growth modestly to just 1.0% in 2023, acknowledging that local economic growth had faltered. It is of note that the RBA's forecasts for domestic growth are now below our own for the first time since 2019.

Australia should still be able to avoid a technical recession due to four key reasons:

1. Australia has been a net beneficiary of global commodity shortages and the prior surge in commodity prices. Commodity prices are now off their peaks, and although they remain very elevated from a historical perspective, the impact of moving through the peak will slow nominal GDP growth quickly over the next six months, removing some of the cushion that has protected corporate profits, tax receipts and wage growth.
2. The household sector continues to hold a significant buffer of excess savings which can be used to smooth consumption growth amid acute cost of living pressures. Nevertheless, our analysis suggests that the residual of the savings buffer skews to older households, leaving younger and more indebted households exposed. As such, we remain particularly cautious on discretionary retail spending.
3. Australia remains incredibly well placed to benefit from the global energy transition. Lithium is already a A\$10bn export industry domestically and Australia is the world's dominant producer. Electric Vehicle sales are forecast to increase 10 times by 2030 and Australia has the world's second largest copper resource. LNG is an important energy transition fuel – it currently accounts for 23% of global electricity generation – and Australia just happens to be the world's equal largest exporter of LNG. The limiting factor nearer term is that escalating costs and project delays risk pushing out the economic benefits.
4. Net migration into Australia contracted in 2021 for the first time since 1945. However, a very strong recovery was recorded through 2022 and a record level of net migration has occurred in recent months, ensuring that Australia's population growth will exceed 2.5% in 2023. This will be the primary mechanism keeping Australia out of recession, yet it comes with the complication of exacerbating the rental shortage evident across all capital cities.

While the RBA has been later than most other developed nations, we believe financial conditions are now firmly in the restrictive zone. While interest rate hikes in Australia will remain a month-to-month proposition, our analysis suggests that the RBA should have concluded its hiking cycle. Moreover, we do expect that the RBA will commence a modest easing cycle in 1H24, most likely commencing in May 2024.

The A\$/US\$ had been under downward pressure as markets grappled with a seemingly more hawkish Fed and a relatively more dovish RBA and poor sentiment on the economic outlook for China. However, with Australia's external accounts remaining in excellent health, our expectation that Australia's economic growth will prove more robust, and the prospect the US\$ down trend will re-emerge as the Fed pivots from its hiking strategy to an easing cycle in early 2024, we expect the A\$/US\$ will appreciate to the low-70s towards mid-2024.

We are most overweight stocks within the Communication Services, Information Technology and Utilities sectors and are underweight Financials, Health Care, and Consumer Staples.

## Client Services

[www.ubs.com/am-australia](http://www.ubs.com/am-australia)

Telephone: (03) 9046 4041

Freecall: 1800 572 018

Email: [ubs@unitregistry.com.au](mailto:ubs@unitregistry.com.au)

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