

UBS Yarra Microcap Fund

September 2022

Fund description

The Fund is an actively managed fund investing in a portfolio of 35 to 65 predominantly Australian Microcap equity securities across a range on industry sectors.

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 strategy

The Portfolio Manager's overarching strategy is to identify those Microcap shares that are believed to be undervalued by the market, based on an assessment of the companies' future cash flows. Normally the Fund will hold between 35–65 stocks in companies with a market capitalisation of generally less than \$250m at the time of initial purchase. The Portfolio Manager searches for businesses that have exposure to growing markets or are benefiting from changes in market structure and are in a rapid growth phase of their life cycle.

Investment return objective

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

Active security positions

Overweight	Underweight
Ridley Corporation	NIB Holdings
Monash IVF Group	New Hope Corporation
Lycopodium	Technology One
GR Engineering Services	Chorus
Alliance Aviation Services	Liontown Resources

Active industry positions

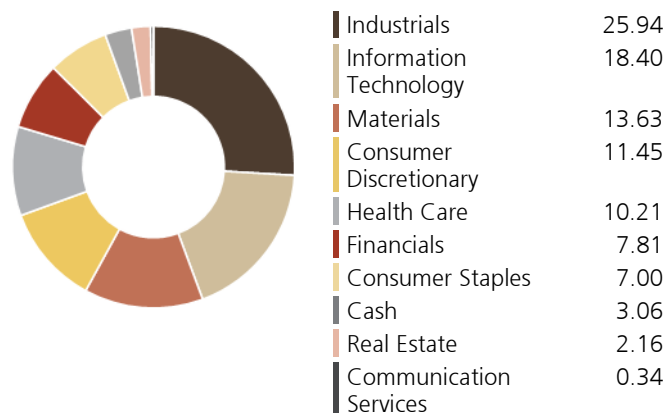
Overweight	Underweight
Capital Goods	Real Estate
Software & Services	Materials
Health Care Equipment & Services	Energy
Food Beverage & Tobacco	Diversified Financials
Transportation	Telecommunication Services

Fund information

Inception date	12 August 2014
Fund size	\$ 56.9 m
Management fee	1.20% pa
Performance fee*	Yes
Minimum initial investment	\$50,000
Typical number of holdings	35 to 65
Distributions	Semi-annually
Buy/sell spread	+/- 0.50%
APIR code	UBS0057AU

* The performance fee equals 20% of the amount by which the Fund outperforms the S&P/ASX Small Ordinaries Accumulation Index.

Fund positioning (%)



Investment performance

Fund	1 month %	3 months %	1 year % pa	3 year % pa	5 years % pa	Since inception* % pa
Total return	(7.15)	3.75	(15.58)	7.08	10.99	12.60
Benchmark**	(11.20)	(0.47)	(22.56)	(0.80)	4.07	5.19
Added Value	4.05	4.22	6.98	7.88	6.92	7.41

*Inception date: 12 August 2014. **S&P/ASX Small Ordinaries Accumulation Index.

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 review

After fees and expenses, the Portfolio declined by 7.71% during the month, outperforming its benchmark by 349 bps.

The largest positive contributors were AVZ Minerals (not held), Lycopodium, and iCollege. AVZ Minerals was suspended from listing pending an announcement regarding their mining and exploration rights at their pre-production Lithium mine in the DRC (Congo). Lycopodium continued to deliver, awarded the services contract for Endeavour Gold Corporation's Sabodala-Masawa Expansion Project. Lycopodium was initially awarded the early works and will now receive the total contract value of over \$26m highlighting their ability to execute and capitalise on this long standing relationship. iCollege was a new addition to the portfolio leveraged to the reopening of Australia, benefiting from the influx of international students attending our universities. The business expects to continue to execute on their growth strategy given the tail-winds emerging in student markets.

The largest negative contributors were New Hope (not held), EnviroSuite and Mincor Resources. New Hope (not held) continued to trade higher on the back of a strong underlying coal price making operations extremely profitable. EnviroSuite traded lower despite no company specific news. Mincor resources was sold off on the back of a lower underlying Nickel price as the possibility of an economic recession, which would significantly hinder the near-term demand outlook for the commodity.

Market review

Australian small caps declined sharply during September with all sectors ending the month in the red.

The S&P/ASX Small Ordinaries Accumulation Index returned -11.2% for the month, taking its 12-month return to -22.6%. In comparison, the broader ASX300 declined -6.3% for the month and, globally, the MSCI World Index fell by 15.7%.

The worst performing sectors were Materials (-14.3%) and Information Technology (-12.4%). In the former, pre-production miners leveraged to the EV thematic plummeted, led by Australian Strategic Materials (ASM, -31.8%), Aurelia Metals (AMI, -25.9%) and RED 5 Limited (RED, -25.5%) In the latter, unprofitable technology companies were noticeable underperformers, in particular Novonix (NVX, -27.3%).

Elsewhere, Real Estate (-12.2%) also experienced widespread declines as the macro-outlook deteriorated. The largest falls came from Centuria Capital (CIP, -16.4%), Arena REIT (ARF, -19.7%) and Cromwell Properties (CMW, -14.5%).

Outlook

Financial markets have now embraced the risk of recession in the US and Europe over the past quarter, and the gap between our more pessimistic forecasts for the global economy and the consensus has narrowed. Indeed, with the Fed signalling that financial conditions are close to neutral, we are edging closer to the point where the pace of monetary tightening will slow, providing some scope for risk markets to recover some lost ground.

The period of excess inflation is starting to recede, with prior surges in commodity prices retreating, an easing in supply constraints, and signs of slowing demand likely to compress elevated sales margins. As central banks continue to await firmer signs that inflation expectations have stabilised and for labour demand to ease, financial markets are faced with the positive news of less restrictive monetary policy and the negative news of likely weaker company earnings.

In a world of heightened concerns of recession in major developed economies, subdued economic activity in China and ongoing conflict between Russia and the Ukraine which has contributed to commodity shortages, high inflation and rising interest rates, the Australian economy presents as a relative safe haven.

Australia's economic data has remained robust in 1H2022, although we do expect economic activity to slow significantly in 2023 to average just 1.5%. While a local recession is possible in 2023, we believe Australia should be able to avoid a technical recession due to three key reasons:

1. Australia has been a net beneficiary of global commodity shortages. This surge in commodity prices saw Australia's export prices in A\$ terms move to their highest levels since the 1880s in 1H2022. The consequence has been strong national income growth, profits growth and an improving underlying fiscal position.
2. The household sector continues to hold a significant buffer of over \$160bn of excess savings relative to pre-COVID levels. Although we expect the impact of higher interest rates and higher living expenses will curtail consumer spending, we do expect the combination of rising wage growth and a run down in the level of savings to continue to support consumption spending.
3. Low levels of spare productive capacity, strong profit and low corporate debt have contributed to robust capital investment intentions.

Over the medium term we believe a recovery in net immigration levels into Australia and Australia's exposure to key commodities crucial to the global energy transition will provide a solid underpin for future economic growth.

While the RBA has been later than most other developed nations in tightening policy, tighter financial conditions in 2022 have come via both significantly higher cash rates, higher government bond yields and wider corporate bond spreads. We expect that the RBA cash rate will finish the year at 3.10%, which we expect will mark the peak for the RBA, well below market expectations of a 4.0% peak in 2H23. The A\$/US\$ has been particularly weak in recent weeks, albeit on a TWI basis the A\$ has been broadly stable. With Australia's external accounts are in their best position since the early 1970s and the prospect the US\$ uptrend will peak as the Fed pivots from its aggressive hiking strategy we expect the A\$/US\$ will appreciate to the mid-70s by end-2023.

Client Services

Telephone: (03) 9046 4041 Freecall: 1800 572 018 Email: ubs@unitregistry.com.au www.ubs.com/am-australia

Any financial product advice in this document is general advice only and has been prepared without taking into account your personal objectives, financial situation or particular needs. Therefore, before acting on any advice, you should consider the appropriateness of the advice in light of your own or your client's objectives, financial situation or needs. Investors should consider the Product Disclosure Statement (PDS) and seek professional financial and taxation advice before deciding whether the product is appropriate for them and whether to acquire, or to continue to hold the investment. Your investment in the Fund does not represent deposits or other liabilities of UBS AG or any member company of the UBS Group including UBS Asset Management (Australia) Ltd (ABN 31 003 146 290) (AFS Licence No. 222605), the issuer and responsible entity of the Fund. Your investment is subject to investment risk, including possible delays in repayment and loss of income and capital invested. The repayment of capital or income is not guaranteed by any company in the UBS Group. Offers of interests in the Fund including the details of the management fee received by the responsible entity are contained in the PDS dated 28 September 2022. The responsible entity has also issued a target market determination (TMD) that describes the class of consumers that comprises the target market for the Fund and matters relevant to its distribution and review. A copy of the PDS (including the PDS additional information booklet) and TMD are available on our website at <https://www.ubs.com/au/en/asset-management.html> or by calling (03) 9046 4041 or 1800 572 018.

The PDS and application form is only available to persons receiving it (electronically or otherwise) while physically in Australia, unless expressly authorised by us in writing. The offer does not constitute an offer or invitation in any place in which, or to any person to whom, it would be unlawful to make such an offer or invitation. The Fund (or the PDS) has not been registered under the laws of any jurisdiction outside Australia. The Fund may not be offered or sold in the United States of America or to 'U.S. Persons' (as defined in 'Regulation S' of the Securities Act of 1933, as amended).

This document may not be reproduced or copies circulated without prior written authority from UBS Asset Management (Australia) Ltd.

Yarra Funds Management Limited (ABN 63 005 885 567, AFSL 230 251) is the portfolio manager of the Fund. The information set out has been prepared in good faith and while Yarra Funds Management Limited and its related bodies corporate (together, the "Yarra Capital Management Group") reasonably believe the investment information and opinions to be current, accurate, or reasonably held at the time of publication, to the maximum extent permitted by law, the Yarra Capital Management Group: (a) makes no warranty as to the content's accuracy or reliability; and (b) accepts no liability for any direct or indirect loss or damage arising from any errors, omissions, or information that is not up to date.

Yarra Funds Management Limited manages the Fund and will receive a fee that is paid from the fee received by the responsible entity and described in the PDS. To the extent that any content set out in this presentation discusses market activity, macroeconomic views, industry or sector trends, such statements should be construed as general advice only. Any references to specific securities are not intended to be a recommendation to buy, sell, or hold such securities. Holdings may change by the time you receive this report. Future portfolio holdings may not be profitable. Past performance is not an indication of, and does not guarantee, future performance.

References to indices, benchmarks or other measures of relative market performance over a specified period of time are provided for your information only and do not imply that the portfolio will achieve similar results. The index composition may not reflect the manner in which a portfolio is constructed. Portfolio characteristics take into account risk and return features which will distinguish them from those of the benchmark.