Investment Commentary
Month to 31 July 2022

Yarra Market Neutral Fund

Net returns as at 31 July 2022

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception* % p.a.
Yarra Market Neutral Fund#	4.40	-2.58	-4.89	8.15	8.42	NA	9.02
RBA Cash Rate**	0.10	0.15	0.22	0.32	0.78	NA	0.90
Excess return (after fees)‡	4.29	-2.73	-5.11	7.83	7.64	NA	8.12

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: August 2016.
# Effective 31 May 2022, Yarra Funds Management Limited was appointed Investment Manager of the Fund. As part of this process, Portfolio Manager Andrew Smith became an employee of Yarra Capital Management, and the name of the Fund was changed from the Karara Market Neutral Plus Fund to the Yarra Market Neutral Fund. Performance prior to 31 May 2022 relates to the Karara Market Neutral Plus Fund. From June 2019, performance figures are those of the Karara Market Neutral PLUS Fund's series 1 units (net of all fees and assumes reinvestment of distributions). Between August 2016 and May 2019, performance is calculated using the actual exit to exit prices of series 1 units of the Ironbark Karara Market Neutral Fund (IKMNF) adjusted for the portfolio construction differences between the two funds as the Karara Market Neutral PLUS Fund security positions are double the size of the security positions held by the previous IKMNF. The effect of management fees of 1.50% p.a., expense recovery of 0.20% p.a. and performance fees of 20% p.a. form part of this calculation. Performance fees include a hurdle rate. Fees are stated inclusive of GST net of RITCs.
** The Fund has minor equity market exposure, with a low volatility target, making an equity index benchmark unsuitable. The Fund profits from stock positioning rather than from equity market moves. The underlying assets of the Fund are of a higher risk profile then cash assets.
‡ Excess return: The difference between the Fund's return and the benchmark return.

Market review

Australian equities rallied sharply during July, following the 9% decline in June, as market expectations increased that interest rate expectations have now peaked.

The S&P/ASX 300 Accumulation Index returned Index returned +5.8% for the month, taking its 12-month return to -2.2%. Globally, the MSCI World Index returned +7.9% in July.

The Information Technology sector was the strongest performer during the period. Within Technology (+15.0%), outperformers included Xero (XRO, +20.8%), Tyro (TYR, +37.5%), Megaport (MP1, +78.0%) and Wisetech (WTC, +33.0%). Other sectors to rally were Real Estate (+12.1%) and Banks (+10.3%), which was led by strong performance from NAB (+11.7%).

The worst performing sector was Metals & Mining (-1.6%) as the commodity complex declined during the period.

Portfolio review

Key Contributors

Long Praemium (PPS) hedged against another domestic platform provider. The position outperformed following Morningstar acquiring Praemium's (PPS) operations in the UK, Jersey, Hong Kong, and Dubai for £35m. This is a significant development, following market speculationg that a potential takeover of Praemium would be more likely.

Long Charter Hall Group (CHC) hedged against another listed fund manager. The position rebounded strongly as long bonds began to fall and investors began to think inflation would be controlled.

Long Genex Power (GNX) received a non-binding indicative takeover offer priced at at 23c per share which represented a 70% premium to where the stock had last traded. Interestingly, GNX was trading at higher levels prior to the end of 2021. The Board knocked back the offer from Skip Capital (Farquhar Family Office) and investors are waiting to see if a higher bid is made.

Long Bubs (BUB) launched a $63m equity raise to help fund its US growth aspirations. The raise follows the US Government seeking international assistance for infant formula supply following a major domestic manufacturer temporarily closing a key manufacturing facility.

Key Detractors

Long Scentre Group (SCG) modestly underperformed a short position held in another domestic retail exposed REIT.

Long Westpac (WBC) modestly underperformed a short position we held in another domestic banking company.

Market 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.

Indeed, 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 heighted 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, and although we do expect economic activity to slow in FY23 we do not expect a recession in Australia 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 $150bn of excess savings (approximately 7% of GDP) relative to pre-COVID levels. Although we expect the impact of higher interest rates and higher living expenses to 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 the key commodities crucial to the global energy transition – including copper, lithium and iron ore – 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 are likely to come via both significantly higher cash rates and a stronger currency. While we expect that the RBA Cash Rate will finish the year at less than 2.5%, below market expectations of 3.0%, the A$ risk continues to skew to the upside. Australia's external accounts are in their best position since the early 1970s, providing an incentive for the A$/US$ to commence an appreciation cycle, together with the attractive carry on offer, improving China economic data and the prospect the US$ uptrend will peak as the Fed pivots from its aggressive hiking strategy. We expect the A$ will finish 2022 at around 76 cents.

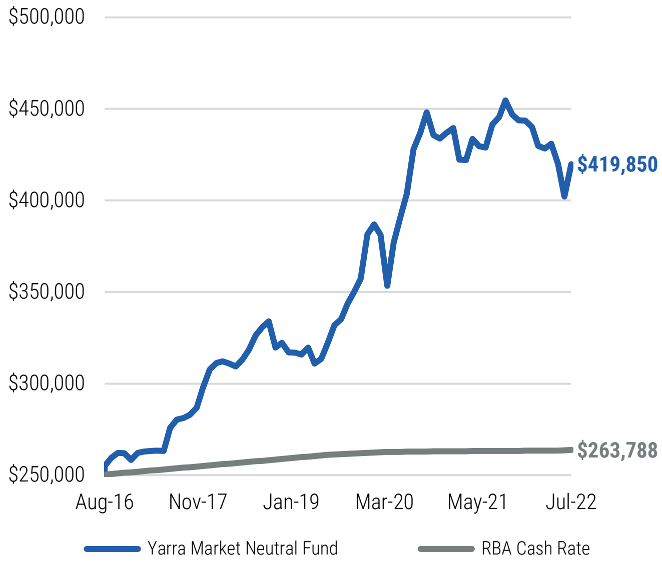
Features

Investment objective	To outperform the RBA Cash Rate (after fees) over rolling 5-year periods.
Recommended investment time frame	Long term, at least 5 years
Fund inception	June 2019
Strategy inception	August 2016
Fund size	A$11.4 mn as at 31 July 2022
APIR code	PER2486AU
Estimated management cost	1.35% p.a.
Performance Fee	20% of excess performance above benchmark (after fees are adjusted to add back any performance fees accrued but not yet paid) provided specified performance hurdle is met
Fund Expense Recovery^	Capped at 0.20% p.a. of NAV
Buy/sell spread	+/- 0.25%

This fund is appropriate for investors with "High" and "Very High" risk and return profiles. A suitable investor for this fund is prepared to accept high risk in the pursuit of capital growth with a medium to long investment timeframe. Please refer to the PDS and TMD for further information.

Investment performance comparison of $50,000

After fees, since inception of the Yarra Market Neutral Fund, August 2016 to July 2022.



For illustrative purposes only. Past performance does not guarantee future results, which may vary. The total net fund returns shown are prepared on an exit to exit basis (i.e. they include all ongoing fees and expenses and assume reinvestment of all distributions). They do not take personal taxation into account. The comparison with the benchmark is for comparative purposes only. Index returns do not allow for transactional, management, operational or tax costs. An index is not managed and investors cannot invest directly in an index. The Fund has minor equity market exposure, with a low volatility target, making an equity index benchmark unsuitable. The Fund profits from stock positioning rather than from equity market moves. The underlying assets of the fund are of a higher risk profile then cash assets.

Applications and contacts

Investment into the Yarra Market Neutral Fund can be made by Australian resident investors only.

Website www.yarracm.com

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