

Yarra Australian Equities Fund

Gross returns as at 31 July 2023

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception* % p.a.
Yarra Australian Equities Fund	3.00	3.01	19.55	15.99	7.68	8.73	10.64
S&P/ASX 200 Accumulation Index†	2.88	2.04	11.67	11.99	7.47	8.31	9.18
Excess return (before fees)‡	0.12	0.97	7.88	4.00	0.22	0.42	1.46

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 July 2023

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception* % p.a.
Yarra Australian Equities Fund	2.92	2.78	18.49	14.96	6.71	7.73	9.64
S&P/ASX 200 Accumulation Index†	2.88	2.04	11.67	11.99	7.47	8.31	9.18
Excess return (after fees)‡	0.04	0.74	6.82	2.97	-0.76	-0.59	0.46

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 Australian Equities Fund: July 1996

† The benchmark for the Yarra Australian Equities Fund has been amended since the Fund's inception. Effective 28 February 2008 the benchmark is the S&P/ASX 200 Accumulation Index, replacing the S&P/ASX 200 ex Property Accumulation Index Monthly. Further information on changes to the Fund's benchmark is available upon request.

‡ Excess return: The difference between the portfolio's return and the benchmark return.

Market review

Australian equities rose in the month of July with almost every sector delivering positive returns.

The S&P/ASX 200 Accumulation Index returned +2.9% for the month, taking its 12-month performance to +11.7%. Similarly, the S&P/ASX 300 Accumulation index generated a return of +2.9% for the month. Globally, the MSCI World Index rose by 3.4%.

The Energy (+8.8%) sector was the strongest performer for the month, with Woodside Energy (WDS, +10.3%) a key contributor to the sector's return. Despite a weak 2Q23 update, Woodside shares still gained as the Brent Crude price rose by ~14% (closing at US\$85/barrel). Another notable stock that benefitted from the commodity's gain was Santos (STO, +5.9%).

July also saw the Financials (+4.9%) sector continue its upwards movement from the prior month. Within the sector, Commonwealth Bank (CBA, +5.4%), NAB (NAB, +7.8%), ANZ (ANZ, +8.6%) and Westpac (WBC, +4.7%) were among the top contributors. The bank sub-sector performed well during the month as the market began to place a higher probability on a soft landing and interest rates to remain higher for a longer period, despite the RBA holding the cash rate at 4.1% following inflation data easing for the second quarter.

Conversely, Health Care (-1.5%) was one of only two sectors to deliver negative returns for the month. The lagging sector return can be mainly attributed to CSL (CSL, -3.2%) as the stock underperformed following the pre-release of lower-than-expected FY24 earnings guidance in June (~10% lower than consensus for group FY24 NPATA).

Portfolio review

Key Contributors

CSL (CSL, underweight) – our underweight to the globally focused biotechnology company contributed positively to performance in July as the stock continued to weaken following the pre-release in June of FY24 group earnings guidance which was below market expectations (around 10% lower than consensus for group FY24 NPATA). The weaker operating outlook was driven by lower growth in its core blood plasma business, Behring, as cost pressures delay the margin recovery story. We retain our cautious outlook for Behring, driven by increased competition, elevated and prolonged cost pressures, adverse relative product growth rates and longer-term product substitution risk. Trading on 28.0 times forward P/E, we retain an underweight position.

United Malt (UMG, overweight) – the global commercial malt processor and distributor outperformed as Malteries Soufflet signed a binding deal to acquire UMG at \$5.00 a share (a +45%

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premium to the undisturbed price) following an extensive period of due diligence.

Sandfire Resources (SFR, overweight) – the copper producer Sandfire was a source of outperformance following the release of its June quarter production report which confirmed a 13% (q/q) production increase at its MATSA copper operations in Spain and total annual production of 99kt. This result was marginally ahead of recently revised guidance and the company expects production will increase to 135kt in FY24 as the newly sanctioned Motheo operation in Botswana ramps up production. We are attracted to copper as a commodity given its leverage to electrification as a key material in batteries and electric motors.

Key Detractors

Iluka (ILU, overweight) – our overweight position in the mineral sands company was a detractor during the month. Despite the company's solid June quarterly production report, ILU expects demand to be softer during 2H23. Competitor Tronox also highlighted this trend which led to market concerns. While we see short-term demand risks, traditional supply sources – particularly in South Africa – appear to be in decline, supporting ILU's expectations for flat pricing in the second half. We continue to favour the mineral sands markets for long-term investment, and specifically ILU as the world's largest Zircon producer and fifth largest producer of titanium feedstocks. Iluka is moving into Rare Earths production through its Eneabba refinery, adding potential for the company to become a critical component producer for the EV industry.

National Australia Bank (NAB, underweight) – the bank sector performed well during the month as the market began to place a higher probability on a soft landing and interest rates remaining higher for longer. We remain underweight, with Australia's banks facing material earnings pressures through declining net interest margins, elevated expense growth and a normalisation in bad debt expenses, meaning sector EPS is likely to be at peak levels.

Tabcorp (TAH, overweight) – the wagering operator underperformed in the lead up to its August result, led by concerns that market turnover has remained soft (likely down 5-10% in 2H23). We continue to see an opportunity over the medium term, and view TAH as a net beneficiary of the upcoming Victorian wagering license tender and regulatory alignment between retail and digital operators. In our view, the company also remains well positioned to benefit from its refreshed TAB25 strategy and gradual consolidation in the sector, which we expect will assist in delivering on the company's medium-term 10% ROIC target.

Key Purchases

Stockland (SGP) – we initiated a position in Australia's largest residential land developer based on a view of the company's capacity to benefit following a peaking of interest rates, quality land assets in key growth corridors across Australia and well-funded financial position. The valuation is supportive, with the stock offering a 6% dividend yield and trading below net asset backing.

Vicinity Centre (VCX) – we increased our position in the shopping mall owning REIT in the period. Key supportive factors include VCX's retail asset mix, with over half its asset base exposed to more advantaged segments of bricks & mortar retailing (i.e. luxury, DFO outlets and recovering CBDs), more resilient in-place leases with high occupancy and fewer holdovers. Additionally, VCX has a strong balance sheet (gearing 25.7% as at Dec-2022) and attractive valuation, with the stock trading at 0.80-times net asset backing and offering a dividend yield above 6%.

JB Hi-Fi (JBH) – we increased our position in the retailer over the period, reflecting our confidence that JBH will continue taking market share to offset the broader weakness in consumer electronics and home appliances. We view JBH as a best-in-class operator that is well positioned to navigate the volatility ahead despite a softening consumer environment, with strong cash generation and a robust balance sheet. Unlike its peers, consensus earnings also already reflect a -26% EPS correction in FY24, resulting in JBH trading at an historical discount which we believe is unwarranted (13.4 times P/E vs. 14.3 times long-term average).

Key Sales

United Malt (UMG) – we exited our position in the global commercial malt processor and distributor after it signed a binding offer with Malteries Soufflet to acquire UMG at \$5.00 a share (a +45% premium to the undisturbed price) following an extensive period of due diligence. With UMG trading close to deal terms, we see limited potential for further outperformance.

Iluka (ILU) – we trimmed a small portion of our position in the mineral sands producer during the period on expectations of a soft 2H23. While the company's June quarterly production report was solid, the company expects some softness in demand during the second half of 2023. Competitor Tronox also highlighted this trend, leading to market concerns. While we see short-term demand risks, traditional supply sources – particularly in South Africa – appear to be in decline, supporting ILU's expectations for flat pricing in the second half. We continue to favour the mineral sands markets for long-term investment, and specifically ILU as the world's largest Zircon producer and fifth largest producer of titanium feedstocks. Iluka is moving into Rare Earths production through its Eneabba refinery, adding potential for the company to become a critical component producer for the EV industry.

QBE Insurance (QBE) – we trimmed our position in the global general insurer following a recent period of outperformance but remain overweight. QBE released a trading update ahead of its full year result, pre-empting concerns on catastrophe (CAT) allowances following storm events in the United States towards the end of half that have impacted peer results. While 2023 will again be impacted by elevated CAT claims, the update highlighted ongoing strength in the underlying business including strong GWP growth and underlying combined ratio expansion.

Key Active Overweights

Reliance Worldwide (RWC) – we view the plumbing supplies company as a compelling opportunity, with the market pricing a significant decline in earnings (P/E of only 14.8 times vs 17.0 times mid cycle) whereas we remain constructive on the through-cycle demand environment given the defensive nature of RWC's revenue base, the majority of which relates to more non-discretionary, repair type housing activity.

Worley (WOR) – we remain overweight the leading provider of global engineering services. WOR's earnings recovery is in its early stages following COVID-19 impacts across FY20-22. Revenue is expected to grow 13-15% in FY23, with leading indicators (Factored Sales Pipeline +36%, Rolling 12 Month Bookings +28%, Backlog +8%) and structural drivers (capital investment required to decarbonise) pointing to strong top-line growth ahead. Margins are also set to accelerate over the coming years as WOR benefits from a more consolidated industry structure, operating leverage, and active mix management.

QBE Insurance (QBE) – the global general insurer remains our preferred insurance exposure, which we expect will deliver strong earnings growth in 2023 and beyond supported by sustained premium rate growth and the beneficial impact of higher interest rates on investment earnings. QBE has substantially improved its underwriting discipline and product focus over the last five years, and we believe it's 11.0 times FY23 earnings multiple excessively discounts the risks inherent in its business model.

Key Active Underweights

CSL (CSL) – we retain an underweight to the globally focused biotechnology company. Underpinning this position is our view that earnings growth from its core blood plasma division (approximately 65% of group earnings) will be more difficult moving forward due to elevated and sticky cost pressures, increased competition, relative product growth rates away from higher margin specialty products and longer-term product substitution risk. While the more recently acquired business, Vifor (now approximately 15% of group earnings) does provide differentiation, we view the business as lower quality than the core plasma franchise. Considering this operating outlook, we do not regard the current valuation (28.0 times forward P/E, 19.2 times EV/EBITDA) as overly attractive at this time.

National Australia Bank (NAB) – we remain underweight the Australian bank reflecting our negative sector view. In our view, Australia's banks are facing material earnings pressures through declining net interest margins, elevated expense growth and a normalisation in bad debt expenses, meaning sector EPS is likely to be at peak levels.

Macquarie Group (MQG) – we remain underweight the stock based on the view the recent earnings uplift is driven by its lower quality and highly cyclical businesses, which we view as unsustainable into the medium term. We see significant downside risk to consensus forecasts beyond FY23, which currently reflects a strong contribution from lumpy items including trading revenue in its commodities business, gains

on sale, performance fees and low loan-loss provisions. We do not expect growth in the more stable businesses will be able to offset this. As a result, we regard MQG's headline forecast P/E multiple of 15.9 times consensus forward earnings as unattractive.

Market 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.

As a consequence, interest rate futures have been quick to price 125 bps of easing in the US through 2024, albeit interest rate futures in most other major economies have merely removed multiple rate hike expectations and adopted a flatter profile through 2024 around current levels rather than actively embedding interest rate reductions.

Moreover, the pessimistic tone of the economic activity data in the US that threatened a technical recession has given way to slightly more update 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.

While negative EPS revisions are likely to persist for several more months, a levelling out in economic momentum and an end to the interest rate tightening cycle will likely provide a shift from bearish equity positioning. Rising bond yields continue to provide the more significant challenge to equity market valuations, albeit the lift in bond yields into mid-2023 can mostly 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 0.3% q/q growth in the March quarter, with much of this growth able to be traced merely to strong population growth and ongoing engineering construction projects. It is clear the prior tightening of monetary policy is having a material impact on the interest rate sensitive parts of the economy. Nominal retail sales have slowed to 0% (six-month annualised), following on from declining volumes in recent quarters. Building approvals continue to decline and are likely to fall further in coming months as declining housing affordability outweighs the impact of an under supplied housing market. Moreover, it is also clear that despite the Federal Budget forecast to return to surplus, government demand growth is waning even faster than private demand growth.

Nevertheless, the good news is that after a pause in the tightening cycle in July, The Reserve Bank of Australia (RBA) remained on hold in August 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.

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 be for nominal GDP growth will slow 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% 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 for the next six months, our bias is that the RBA should have concluded its hiking cycle. However, we do expect that the RBA will commence a modest easing cycle in 1H24.

The A\$/US\$ had been under downward pressure as markets grappled with a seemingly more hawkish Fed and a relatively

more dovish RBA. However, the RBA has recently sounded more hawkish than the Fed the A\$ has started to appreciate. 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 persist as the Fed pivots from its hiking strategy to an easing cycle in early 2024, we expect the A\$/US\$ will appreciate to the mid-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.

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	11.40	4.05	7.35
Consumer Discretionary	7.35	6.49	0.86
Consumer Staples	0.00	4.70	-4.70
Energy	5.71	5.62	0.09
Financials	20.69	28.43	-7.74
Health Care	4.11	9.30	-5.19
Industrials	8.21	7.05	1.16
Information Technology	8.31	2.55	5.76
Materials	24.28	24.20	0.08
Real Estate	3.90	6.08	-2.18
Utilities	2.96	1.54	1.42

Top 5 holdings

	Portfolio %	Benchmark %	Active %
BHP	10.74	10.65	0.09
Commonwealth Bank of Australia	5.96	8.14	-2.18
Woodside Energy	5.71	3.29	2.41
Westpac Banking	4.63	3.58	1.04
Telstra	3.75	2.25	1.50

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
Reliance Worldwide	2.96	0.15	2.81
Worley	2.88	0.30	2.58
QBE Insurance	3.57	1.07	2.50
Underweights			
CSL	1.42	5.92	-4.50
National Australia Bank	0.00	4.07	-4.07
Macquarie Group	0.00	2.90	-2.90

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	12.24	2.51	-6.24	-2.00
Distribution return	6.25	12.45	12.95	9.72

The Growth Return is measured by the movement in the Fund's unit price (inclusive of fees), 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 companies listed on the Australian Securities Exchange. In doing so, the aim is to outperform the S&P/ASX 200 Accumulation Index over rolling 3-year periods.	
Recommended investment time frame	5 - 7 + years	
Fund inception	July 1996	
Fund size	A\$112.3 mn as at 31 July 2023	
APIR codes	JBW0009AU	
Estimated management cost	0.90% p.a.	
Buy/sell spread	+/- 0.15%	
Platform availability	Asgard Ausmaq BT Panorama BT Super Wrap FirstWrap GrowWrap	Hub24 IOOF Pursuit Macquarie Wrap Netwealth Oasis Powerwrap

Investment performance comparison of \$50,000

After fees, since inception of the Yarra Australian Equities Fund, July 1996 to July 2023.



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 S&P/ASX 200 Accumulation Index 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. Note that the minimum initial investment amount for the Yarra Australian Equities Fund is \$10,000.

Applications and contacts

Investment into the Yarra Australian Equities Fund can be made by Australian and New Zealand resident investors only.

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