YARRA CAPITAL MANAGEMENT

Yarra Growth Fund

Net returns as at 31 March 2024

	1 month %	3 months %	6 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception % p.a.
Total Fund return (net)	3.09	11.24	15.36	16.18	7.63	7.54	7.70	7.06
Fund growth return (net)	3.09	11.24	14.71	14.45	4.58	2.70	0.88	1.80
Fund distribution return (net)	0.00	0.00	0.64	1.72	3.05	4.84	6.82	5.27
Benchmark*	2.65	8.33	14.49	17.87	9.37	9.32	9.41	8.33

Source: YFML, Citi. Total Fund net returns are post fees, pre tax using redemption prices and assume reinvestment of distributions. Fund growth return is the change in redemption prices over the period. Fund distribution return equals Total Fund minus Fund growth return. Past performance is not an indicator of future performance. Inception date: February 1996.
* The Fund's benchmark is a composite index constructed using the applicable asset class index, weighted according to the Fund's benchmark asset allocation of: 15% of Bloomberg AusBond Composite 0+ YR Index for Australian fixed interest, 30% of S&P/ ASX 200 Accumulation Index for Australian shares, 50% of MSCI All Countries World Index Net Total Return AUD Index (unhedged) for overseas shares, 0% of S&P/ASX 300 Australian Real Estate Investment Trusts (A-REITs) Accumulation Index for property securities (effective 16 December 2013. Prior to this was the S&P/ASX 200 A-REITs Accumulation Index), and 5% of Bloomberg AusBond Bank Bill Index for Cash.

Portfolio review

The Fund returned 11.24% for the quarter, outperforming its composite benchmark return of 8.33% by 291 basis points (bps).

Australian Equities

The Fund's allocation to Australian equities outperformed the broader market during the quarter. The S&P/ASX 200 Accumulation Index returned 5.33% over the same period.

The Fund's Australian Equities allocation is invested in the Yarra Australian Equities portfolio and the Tyndall Australian Share Wholesale portfolio. The Yarra portfolio outperformed the index this quarter, while the Tyndall portfolio underperformed.

All sectors posted gains during the quarter, except for materials, which dropped by 6.20%. The decline in the materials sector was largely due to falling iron ore prices.. Information technology was the best performing sector up 24.36%, driven by global enthusiasm for AI. Real estate (15.31%), consumer discretionary (12.88%) and financials (12.03%) outperformed the broader market, suggesting consumers and businesses were more resilient than previously thought and the Australian economy might be more immune to the previously feared cyclical risks.

The largest relative contributors to performance were Reliance Worldwide, NextDC, ResMed, QBE Insurance and JB Hi-Fi. The plumbing supplies company Reliance Worldwide outperformed with an encouraging 1H24 result ahead of consensus driven by the core Americas division. NextDC reported a solid 1H24 result with contracted capacity of 149MW. ResMed outperformed after releasing its second-quarter results, reporting a 12% increase in revenue, which exceeded consensus expectations. Despite the focus on GLP-1 risk, the investment manager forecasts that ResMed will deliver another quarter of robust top line growth, driven by masks/accessory sales. QBE delivered a solid full year result in February, highlighting continued healthy premium growth across core product lines, decent unit growth and ongoing de-risking of the North American and property businesses. JB Hi-Fi outperformed following release of its 1H24 results.

The largest detractors to relative performance over the quarter were Goodman Group, Sims, Wesfarmers, Nine Entertainment and National Australia Bank (NAB). An underweight position in Goodman Group negatively impacted performance, as the company's shares performed exceptionally well after it released its half-year results. The result was stronger than expected which led to a modest EPS guidance upgrade for FY24. However, this upgrade still fell short of the market consensus. Sims underperformed following a weak 1H24 result driven by lower metal trading margins and inflationary pressures. The underweight position in Wesfarmers detracted from performance following a strong result from Kmart, which came in ahead of market expectations. Nine underperformed following release of its 1H24 result, guidance signals a deterioration in 3Q from 1H trends driven by metro FTA (Free-to-Air) and radio broadcasting. The underweight position in NAB contributed to underperformance. NAB's share price hit a 52-week high during the period, reflecting expectations that the Australian economy might achieve a soft landing in the next 12 months.

Global Equities

The Fund's Global Equities allocation outperformed over the quarter. The MSCI AC World Index, measured in AUD and unhedged, recorded a gain of approximately 13.16%, outperforming most asset classes during this period.

The Fund's Global Equities allocation primarily invests in the

Yarra Global Share Fund, with a smaller portion in the Yarra Global Small Companies Fund. Both funds outperformed the index during the quarter.

Developed market equities had a strong quarter thanks in large part to the performance of growth stocks. This was especially true in the US, where the S&P 500 was driven higher by AI related stocks especially those within the communications services and information technology sectors. While some European equity indexes, such as the French CAC 40, reached new all-time highs, European equities overall continued to lag the US and Japan, with the MSCI Europe ex-UK Index posting below par returns. European stocks did, however, end the quarter on a brighter note as global investors, concerned about the sustainability of returns in the US, turned to Europe where lower valuations attracted a catch-up trade. UK equities lagged most of their international peers, suffering from its value bias, as well as from the poor performance of the UK economy. Emerging markets significantly underperformed their developed market peers as investors remained concerned about China's growth prospects.

Key contributors to performance included Nvidia Corporation, Palomar Holdings., and Meta Platforms. Nvidia shares continued to climb higher as the company hosted its semi-annual GPU technology conference, which highlighted the significant runway for AI adoption and NVIDIA's central positioning within this ecosystem. Palomar continued to outperform following the release of strong FY23 results in February. Meta performed strongly on the back of better-than-expected quarterly results. The pivot in capex instigated last year and the conscious decision to reinvest in core Facebook platforms (Reels) have increased user engagement and driven a sharp acceleration in advertising revenue.

Notable detractors to performance over the quarter included HDFC Bank, Sony and Amadeus. HDFC shares struggled in the quarter as concerns over short-term margins, growth and merger-related weakness dominate sentiment around the stock. Taking a longer view, management plan to prioritise profitability over growth, and given the quality of HDFC Bank's franchise, we have confidence that they can alleviate margin pressure by gathering lower-cost deposits to replace some of their expensive borrowing. Sony struggled to perform after the company published lacklustre medium-term guidance and continues to expect structural challenges in the gaming segment to dampen profit growth. Amadeus struggled to perform as investors feared that an accelerated decline in the use of travel-booking services would challenge the outlook for the company. Despite these concerns, the company published results that were in-line with market expectations and provided an encouraging outlook, supported by strong commercial momentum from new contracts.

Australian Fixed Interest

The Fund's Australian fixed interest allocation underperformed marginally over the quarter. The Australian bond market (as measured by the Bloomberg AusBond Composite 0+ Yr Index) returned 1.03%.

The Fund held an overweight duration position over the quarter which turned out to be neutral for performance amid volatile bond yields. Market sentiment on rate cut timings continued to shift, influenced by economic data and central bank rhetoric. Profit-taking in the previous quarter on an increased overweight duration position mitigated the impact of yield volatility on the Fund.

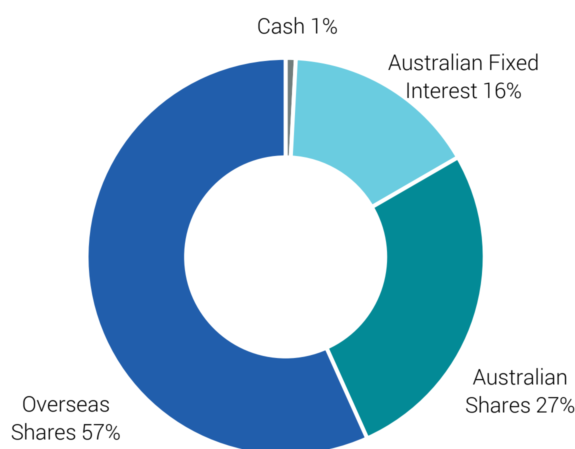
The Fund's curve position benefited from curve steepening during the quarter, although to a lesser extent than in the previous quarter. Anticipating significant steepening of the yield curve once the RBA initiates rate cuts, the fund aims to capitalize on opportunities to increase its curve steepening position. This strategy aligns with expectations of future cash rate movements.

Sector allocation favouring credit, particularly in financials within the 0-5 year maturities, alongside senior RMBS/ABS securities, contributed positively to performance. Narrowing semi-government spreads provided additional support to performance. The fund's higher-than-benchmark running yield, driven by supranational and credit securities, also contributed to performance.

Strategic Asset Allocation

Asset Class	Target Allocation (%)	Range (%)
Australian Shares	30	20-45
International Shares (unhedged)	50	35-65
Property Securities	0	0-10
Total growth assets	**80**	**70-95**
Australian Fixed Interest	15	5-25
Cash	5	0-20
Total income assets	**20**	**5-30**

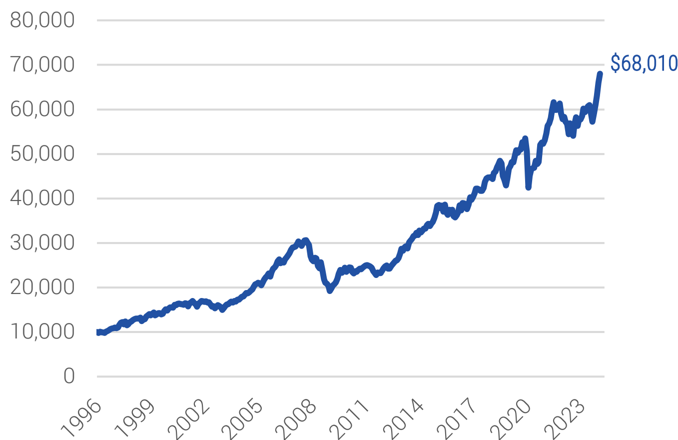
Asset Allocation at Quarter End



Source: YFM, Citi

Performance Graph

Value of $10,000 invested in the Yarra Growth Fund since inception:



Source: Citi & YFM. Past performance is not an indicator of future performance.

Market Outlook

Optimism continues to be driven by financial markets becoming increasingly convinced that central banks are now preparing to ease interest rates from mid-2024.

Good news on inflation has also been met with signs of economic resilience. Although Europe continues to toy with a technical recession, the strength of the recovery in Emerging Market industrial production bodes well for a recovery in European demand in 2024, and indeed survey evidence suggests a recovery in European demand has commenced. This strength in Emerging Market growth has largely been in spite of China rather than because of China. Nevertheless, the bout disinflation in China has largely run its course and economic data has become more mixed/positive rather than universally poor. We continue to expect China to deliver on a more meaningful infrastructure package in 2024 and further encourage credit expansion to the real economy which should underpin economic growth around 5% in 2024 – a target that the Chinese government also adopted in recent weeks. As such we expect China to begin to provide a more meaningful support to global economic growth as we move through 2024.

Turning to Australia's prospects despite a weak finish for economic growth in 2023 – expanding just 0.2%qoq and 1.5%yoy - we continue to suggest that not only will Australia avoid a recession it will likely accelerate sequentially through 2024 with the improving global backdrop acting as a tailwind. No one should be disputing that 2023 likely felt like a recession for many Australians. A per capita recession and a negative income shock for those with high debt and young families has cascaded into weak discretionary spending as high interest rates coalesced with surging insurance, utilities, rates, education, and food prices. Nevertheless, economic growth was held up by several unusual features this economic cycle vis-à-vis prior cycles;

1. Commodities. Prior commodity price strength continued to underwrite double digit nominal economic growth and profitability.
2. Backlogs. Much has been made of the backlog of work in housing construction that has nullified the typical cyclical shock that is transmitted via the housing construction sector during rate hiking cycles. Approvals and affordability are at very poor levels yet the level of home building has barely declined at all. The backlog in work yet to be done is now peaking at a very high level suggesting we shouldn't be looking at the housing sector as a source of new economic growth, but equally we shouldn't be expecting a precipitous collapse in 2024. That may come in 2025 if interest rates remain at current levels, but that is not our expectation. But less has been made of the backlogs in non-residential building (led by offices, warehouses, health and transport) which equates to 7% of GDP and the backlog of engineering construction (led by roads, railways, electricity and mining which equates to 16% of GDP. This enormous backlog of work has kept upward pressure on the labour market and on input prices at a time when typically a global slow down would have seen investment tumble between 10-15%.
3. Buffers and Asset prices. Newly indebted households without other forms of income producing assets feel the full force of rate hikes. However, the economy wide impact of interest rates is diluted the more that growth in income producing assets outstrip the growth in debt. The rising trend in net household assets as a share of income over time means that income from term deposits, financial assets and investment property ownership have all risen over time and all produce an income stream which even after 13 rate hikes this cycle is still in excess of the rise in interest payments on the outstanding debt. This explains the bifurcated nature of spending growth. Older asset rich households are largely impervious to the rate hikes and as such luxury spending categories remain strong whereas younger indebted households cashflow has turned negative and spending is being seriously challenged. In aggregate a rate hike pack less of punch compared to prior cycles but the young and indebted are taking a disproportioned beating.
4. Population pump priming. Net immigration has surged well through government projections taking population growth close to 2.5%yoy growth in 2H23. Quite simply, it is very hard to record a recession with that type of population growth at your back. We do expect net migration to slow in 2024 as the government seeks to tighten up some education programs and entitlements, yet the risk remains that the flood of people entering Australia surprises on the upside until a more material rise in the unemployment rate is realised.

Some additional factors are worth noting that support a more positive outlook into 2024 and beyond.

1. Commodity prices are rising again. A falling USD and stronger global demand have seen commodity prices rising in Q4 which will provide a fillip for profits, tax revenue and nominal economic growth.
2. Fiscal support and tax cuts. Despite a change to the details of the Stage 3 income tax cuts, the package is equivalent to 1.0% of disposable income. In conjunction with the Federal Budget in surplus, the RBA rate cycle likely complete and an election looming in 2025 it is likely that addition fiscal support will be announced in 1H24 to support lower and middle income households.
3. Inflation moderation to drive rate cuts. We expect inflation to move into the top of the RBA target band before the end of 2024, setting up the prospect of the RBA easing in August and again in November 2024. While we are expecting a shallow rate easing cycle it will likely come earlier than most expect and importantly the RBA has renewed firepower to drive a more powerful economic recovery should inflation surprise on the downside.
4. Capex intentions have lifted. We were pleasantly surprised to see that the ABS measure of investment intentions rose through 2H23 and now suggests business investment will rise 10% in 2023-24 – well above the RBA's 1-2% forecast. Indeed, not only has business investment been robust, but there are also signs it is accelerating.

Consequently, we are relatively optimistic on the outlook for the Australian economy and constructive on the equity market outlook for 2024. We expect economic growth to average 2.25% v a consensus forecast of 1.5%, bond yields to finish the year at 4.0%, the $A/$US to reach 74c, and Australian equities to return 10% in in large caps and 15% in small caps. We are most overweight stocks within the Utilities, Information Technology, and Industrials sectors, and are underweight Financials, Consumer Staples and Health Care.

Fund Objective

The Fund aims to provide a modest level of capital growth and income over the medium to long-term, with total returns (before taxes, fees and expenses) above the Fund's benchmark over rolling five-year periods.

Key Facts	
Responsible Entity Yarra Funds Management Limited	**Management Cost** 1.15% p.a.
APIR Code SUN0021AU	**Buy/Sell Spread** 0.15%/0.15%
Fund Size A$76 mn as at 31 March 2024	**Distribution Frequency** Half Yearly
Minimum Investment AUD 2,000	

Contact Us

Yarra Capital Management
Level 19
101 Collins Street
Melbourne VIC 3000, Australia

Phone (Australia) 1800 034 034
Phone (Overseas) +61 3 9002 1980
Email IST@yarracm.com
Website www.yarracm.com

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