YARRA CAPITAL MANAGEMENT

Investment Commentary
Quarter to 30 June 2025

Yarra Australian Smaller Companies Fund

Gross returns as at 30 June 2025

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	Since inception* % p.a.
Yarra Australian Smaller Companies Fund	1.62	7.32	13.21	12.66	N/A	10.06
S&P/ASX Small Ordinaries Accumulation Index	0.85	8.62	12.26	9.99	N/A	5.79
Excess return (before fees) ‡	0.77	-1.30	0.95	2.67	N/A	4.27

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 30 June 2025

	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	Since inception* % p.a.
Yarra Australian Smaller Companies Fund	1.55	7.09	12.25	11.71	N/A	9.14
S&P/ASX Small Ordinaries Accumulation Index	0.85	8.62	12.26	9.99	N/A	5.79
Excess return (after fees) ‡	0.70	-1.53	0.00	1.72	N/A	3.35

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 Smaller Companies Fund: August 2020.

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

Market review

The Australian small caps market strengthened during the second quarter of 2025.

The S&P/ASX Small Ordinaries Index returned +8.6% for the quarter, taking its 12-month return to +12.3%. Similarly, the broader S&P/ASX 300 Accumulation Index returned +10.8% for the period whilst, globally, the MSCI World Index also increased, returning +9.5% for the quarter.

Materials (+6.6%) was the largest contributing sector as a number of stocks including Brickworks (BKW, +43.1%), De Grey Mining (DEG, +15.5%) and Genesis Minerals (GMD, +15.9%) outperformed. This was somewhat offset by falls in Nufarm Limited (NUF, -37.7%), Ora Banda Mining (ORA, -29.8%) and Bellevue Gold (BGL, -21.4%).

The Industrials sector (19.9%) was the second largest sector contributor with DroneShield (DRO, 151.9%), Ventia Services Group (VNT, +28.9%) and Austal (ASB, +49.9%) gaining.

Within the Financials (+11.3%) sector Zip Co. (ZIP, +90.7%) and Netwealth Group (NWL, +31.5%) posted strong gains.

Returns were mostly positive within the Real Estate sector (8.0%) with PEXA Group (PXA, +21.9%), Charter Hall Group (CHC, +12.2%), Region Group (RGN, +9.6%) rising.

The only sector to post a negative return was Health Care (-4.3%) with Mesoblast (MSB, -15.6%), Botanix Pharmaceuticals (BOT, -29.7%) and Monash IVF Group (MVF, -37.9%) posting losses. Monash IVF's share price suffered losses following a highly publicized incidents of embryo's being mixed up.

Portfolio review

Key Contributors

Megaport (MP1, overweight) – the network software company outperformed during the period despite no material company specific news. Megaport is exposed to high-growth end markets in cloud and AI, with revenue growth supported by market share gains driven by new products, improved execution, and challenges faced by key competitors. We view the cost base as sustainable following several years of reinvestment in product and distribution. We expect the net cash balance sheet to continue strengthening, supported by increasing positive free cash flow generation.

Kelsian Group (KLS, overweight) – the transport service company outperformed during the period after it reiterated FY25 earnings guidance at the lower end of the prior range. We remain positive on Kelsian; we believe the Australian bus business will continue to generate earnings growth, supported by the defensive nature of existing contacts with cost pass through provisions, new contract additions and improved staff availability. The US bus business has a strong demand outlook from new and existing customers, with pricing increases to offset cost inflation and the opportunity to redeploy capital from lower returning Marine and Tourism assets to industry consolidation opportunities.

Netwealth Group (NWL, overweight) – the leading independent wealth management platform outperformed during the period as rising equity markets created a positive environment for flows and upside to FY26 earnings estimates. We view NWL as a very high quality, high growth business with a long pathway of growth ahead, in particular through market share expansion.

Key Detractors

Bellevue Gold (BGL, overweight) – the gold producer underperformed during the period following its updated production guidance and equity raising. The equity raise proceeds will help de-risk operations and provide working capital to close out near-term hedges, providing greater leverage to the gold price and stronger free cashflow generation. We retain our positive view on the company, and are attracted to the high-grade Bellevue Gold Mine, upside to reserves, and future production from further exploration.

Zip Co (ZIP, underweight) – the buy now pay later (BNPL) company outperformed following the announcement of its second quarter of positive group cash EBTDA, driven by record-low credit losses in its core Australian business and rapidly improving margins in the US. The news was compounded by RBA interest rate cuts, which lowered the company's funding costs, leading Zip to upgrade its full-year profitability guidance.

Imdex (IMD, overweight) – the mining services company underperformed during the period following a trading update that indicated a slight delay to the expected cyclical recovery. We continue to hold a positive view towards Imdex given cyclical upside in exploration spending globally, continued long term market growth from critical metals demand growth and the growing difficulty in finding new resources. Furthermore, there is a significant global market share opportunity from organic and acquired technologies such as Devico. Valuation upside remains attractive given the strong growth outlook and conservative accounting.

Market Outlook

Another month of heightened geopolitical tensions in June did little to dent risk appetite. The S&P/ASX 200 returned +1.4% for the month, building on the +4.2% surge in May. However, Small Caps and REITs lagged the ASX200, returning +0.8% and +0.5%, respectively.

Global equities rose +1.9% in June in unhedged A$ terms, however, a strong +2.3% A$ rise in the month eroded a +4.3% return in the month that was available for hedged global equities. The strong A$ rise was aided by US dollar weakness and a bounce in commodities which returned +4.5% in June.

Gold returned a more modest +0.4%, following a flat May. Despite two relatively modest months, gold has delivered a return of +26% in 1H25 and +42% over the year, easily the best performing asset class.

In fixed interest markets, global bonds returned 1.9% in June and 4.5% for the quarter, whereas Australian fixed interest returned a more modest 0.7% return in June and 2.6% for the quarter. Within Australian fixed income markets, government bonds were the best performing in June, returning 0.8% for the month.

Ranking 1H25 returns reveal that, excluding gold, hedged global equities led the way with a +9.5% gain. The S&P/ASX 200, S&P/ASX Small Ordinaries and the A$ each returned +6.4% over the same period. This reinforces our suggestion since the start of 2025 for investors to consider hedging international equity exposure in 2025. Notably, global bonds returned an impressive +7.3% in 1H25, easily eclipsing the +4% return from local bonds, despite ongoing fears of unstainable US fiscal debt accumulation.

Locally, Australia's fragile economic recovery again disappointed in the March quarter, with subdued consumption holding economic growth to +0.2% (q/q) and +1.3% (y/y). However, we believe that the RBA has now set its course to return interest rates to a neutral setting and will ultimately deliver a deeper rate cutting cycle than expected. Our rationale is that the RBA's assessment of the 'neutral rate' of interest has been lowered by around 50 bps and, combined with the RBA now forecasting underlying inflation to be around the mid-point of the inflation target throughout its forecasts, it is clear that the RBA in now setting to reduce interest rates at a regular cadence until it approaches the 'neutral' rate.

It is also worth noting that that the RBA has adopted an optimistic assumption for China's ability to withstand a trade war with the US and has put more weight on the currency as a transmission path for monetary policy. The implication being should China's growth data falter, or the A$ appreciate meaningfully, then the case for earlier and deeper rate cuts can be made.

This is good news for Australian-based risk assets. We believe the main beneficiaries will be the housing construction and consumer sectors of the economy. However, the unusual combination of the prospect of lower interest rates and a higher A$ could provide powerful amplifying effect for smaller companies and will likely sustain offshore interest in Australian assets exposure. Should US economic data continue to soften in coming months, Australia looks well placed to benefit from both an economic and financial market perspective.

We are most overweight stocks in the Financials, Information Technology and Industrials sectors and are underweight Consumer Discretionary, Energy and Communication Services.

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	2.54	6.41	-3.87
Consumer Discretionary	8.40	14.24	-5.84
Consumer Staples	0.97	2.57	-1.60
Energy	2.26	7.14	-4.88
Financials	18.77	13.15	5.62
Health Care	7.94	4.99	2.95
Industrials	13.62	9.43	4.20
Information Technology	10.28	6.00	4.28
Materials	21.06	24.32	-3.26
Real Estate	10.27	11.77	-1.50

Top 3 holdings

	Portfolio %	Benchmark %	Active %
Gold Road Resources	4.66	1.27	3.39
Netwealth Group	3.96	1.51	2.46
Auckland International Airport	3.94	0.99	2.95

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
Gold Road Resources	4.66	1.27	3.39
Pinnacle Investments	3.29	0.00	3.29
Megaport	3.90	0.83	3.07
Underweights			
Ventia	0.00	1.56	-1.56
Capricorn Metals	0.00	1.48	-1.48
Zip Co	0.00	1.44	-1.44

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.

Features

Investment objective	To achieve medium-to-long term capital growth by investing in a diversified portfolio of smaller Australian companies. In doing so, the aim is to outperform the S&P/ASX Small Ordinaries Accumulation Index over rolling 3-year periods.
Recommended investment time frame	5 - 7 + years
Fund inception	August 2020
Fund size	A$95.2 mn as at 30 June 2025
ARSN code	642 665 263
Estimated management cost	0.85% p.a.
Buy/sell spread	+/- 0.30%

Disclaimers