YARRA CAPITAL MANAGEMENT

Yarra Australian Equities Fund

Gross returns as at 31 May 2024

	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	-0.42	0.61	7.57	7.53	8.06	7.24	10.42
S&P/ASX 200 Accumulation Index†	0.92	1.16	12.93	6.80	7.82	7.78	9.19
Excess return (before fees)‡	-1.34	-0.55	-5.36	0.73	0.24	-0.54	1.23

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 May 2024

	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	-0.50	0.38	6.61	6.57	7.09	6.25	9.42
S&P/ASX 200 Accumulation Index†	0.92	1.16	12.93	6.80	7.82	7.78	9.19
Excess return (after fees)‡	-1.41	-0.78	-6.32	-0.23	-0.73	-1.53	0.23

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

The Australian Equities market was positive for the month of May.

The S&P/ASX 200 Accumulation Index returned 0.9% for the month taking its 12-month return to +12.9%. Comparatively, the S&P/ASX 300 Accumulation Index generated a +0.9% return, and globally, the MSCI World Index jumped by 4.2%.

The largest sector contributor was Financials (+2.6%) with the big four banks performing strongly, having shaken off earlier concerns following higher than expected CPI results. Commonwealth Bank (CBA, +4.4%), National Australia Bank (NAB, 2.8%), Westpac (WBC, +3.5%) and ANZ (ANZ, +3.3%), all saw their share prices rise over the period.

Information Technology (+5.5%) also outperformed during the month, with Xero (XRO, +10.6%) the main driver of performance following stronger than expected FY24 results. NextDC (NXT, +6.6%) and WiseTech Global (WTC, +4.2%) also rose during the period.

In contrast, Communication Services (-2.6%) was the worst performing sector, with Telstra (TLS, -5.5%) the main detractor during the period. The Australian telco saw its share price decline during the month as it announced its intention to reduce its workforce numbers as part of wider restructuring.

Portfolio review

Key Contributors

Pexa (PXA, overweight) – the online property exchange platform outperformed following its announcement of a strategic partnership with UK bank NatWest. The partnership will see the lender utilise PEXA's world-leading digital property exchange technology to deliver 48-hour remortgage transactions to its customers. PXA remains attractive as it has increased its focus on productivity enhancements in the base business and is strategically reducing cash flow drag from investments in the international and digital growth segments.

Xero (XRO, overweight) – the SaaS provider of cloud accounting, payroll and payment solutions outperformed the market following the release of its FY24 results. XRO benefited from strong revenue growth, cost controls and earlier achievement of the Rule of 40 target. The outlook for further revenue growth is strong given better exit-ARPUs, and the continued migration onto the cloud. The company has made considerable inroads over the last 12 months in improving its US product and go-to-market strategy in the US. The market also liked XRO's plan to grow more efficiently in the future, and better balancing investment in the business and providing FCF return to investors.

James Hardie (JHX, underweight) – the leading building materials supply company underperformed during the period driven by the release of the fourth quarter and full year update. Driving the weakness was the company missing fourth quarter profit expectations by 3%, with product sold into its core US market falling short by 1%. In addition, JHX's guidance for FY 2025 was well below the consensus estimate (-13% below). We retain an underweight position as we note an increasingly challenged market share outlook, particularly given the excellent year in FY 2024 for share gains. Indeed, guidance implies a massive contraction from 11% primary demand growth in FY24 to 2% FY25.

Key Detractors

Bapcor (BAP, overweight) – the auto parts retailer underperformed during the period following the release of a weak trading update (-18% EPS downgrade to FY24 consensus) and an announcement that incoming CEO Paul Dumbrell was no longer joining the company. Although revenue was only modestly weaker, margins were impacted by operating deleverage and cost pressures. With the stock trading at a discount to history (14.2 times FY25 P/E vs 18.2 times 10-year average), the valuation does not capture the defensive quality of BAP's trade and wholesale business despite some near-term uncertainty.

Tabcorp (TAH, overweight) – the wagering operator underperformed during the period with limited company specific news but reflected a broader de-rate in consumer-exposed businesses. TAH has been impacted by weaker conditions in the domestic wagering market and operating deleverage, with turnover down -4% across both retail and digital channels coupled with a step up in opex. While trading has remained soft in 2H24, TAH have retained share and will benefit from a market recovery as consumer pressures moderate.

Sims (SGM, overweight) – the steel producer underperformed following an operational update that disappointed relative to expectations. The company expects to report an underlying 2H EBIT marginally lower than that achieved in 1HFY24. The outlook for SGM near term remains tough given China continues to over-produce steel and export the excess, but with the stock trading below NTA, and evidence that NAM is finally turning a corner, we are happy to retain our overweight position.

Key Purchases

Bapcor (BAP) – we added to our existing position the automotive supplier, reflecting our view that BAP's trade and wholesale businesses remain attractive despite a period of management turnover. While Autobarn has been impacted by a softer consumer, Bursons retains an entrenched position within the aftermarket category. With the stock trading at a discount to history (14.2 times FY25 P/E vs 18.2 times 10-year average), the valuation does not capture the defensive quality of BAP's trade and wholesale business despite some near-term uncertainty.

Incitec Pivot (IPL) - we added to our position in IPL following the company's 1H24 result. The company should soon conclude the sale process for its Fertiliser division. A resolution either way on the sale process will allow the company to commence it's $900m buyback (16% of $5.8bn market cap). The outlook for Dyno Nobel is strong given trends in the global explosives markets. In addition, IPL have announced a largely capital light plan to lift ROIC from 5.1% to double digits.

Key Sales

ResMed (RMD) – we trimmed our RMD position back to target active weight reflecting the attractive upside that remains from increasing the penetration rate of CPAP into deep-demand markets globally, demonstrating operating leverage and seeing the current stock multiple trade back closer to its long-term average (currently 25 times P/E vs 29 times LTA).

QBE Insurance (QBE) – QBE remains a key long position in the portfolio, with continued operating execution and ongoing robustness in the rate cycle supporting increases in the share price. Reflecting some of the recent outperformance, we took the opportunity to trim the position.

Reliance Worldwide (RWC) – following strong recent performance, we have trimmed the RWC position. Recent increases in input costs (copper) and a US R&R market that is yet to turn positive (higher rates) are likely to limit positive earnings surprises in the near term, however we remain supportive of the medium and long-term opportunity of the cyclical industrial trading on an attractive multiple (15 times P/E NTM vs 17 times LTA).

Key Active Overweights

ResMed (RMD) – we remain overweight the medical equipment company which we view as the most attractive large-cap healthcare company on the ASX today. The stock has sold off due to concerns around a range of factors including the impact on its installed base of CPAP devices following the emergence of weight loss drugs (GLP-1s), recent gross margin slippage versus expectations and competitive landscape changes (Philips remains out of the market on hardware in the USA). We are not as bearish on these issues, with our favourable view predicated on RMD's large and underpenetrated market (sleep and COPD (chronic obstructive pulmonary disease), clear operating leverage over time (SG&A and R&D) and its strong track record of capital deployment as the business shifts further into digital, connected care solutions.

Woodside Energy (WDS) – we are overweight the oil and gas producer. The company has lagged rising oil and LNG prices in recent months and, in our view, is undervalued. We are attracted to the company's strong growth profile from new projects that remain on budget and schedule to increase production by more than 30% over the next two years.

Reliance Worldwide (RWC) – we view the plumbing supplies company as a compelling opportunity, with cyclical upside as end-markets recover over the period ahead and improved product mix rolls out. We believe this valuation doesn't give appropriate credit to the mid-cycle earnings power of the

group considering the resilience of its end markets, the majority of which relates to more non-discretionary, repair type housing activity.

Key Active Underweights

National Australia Bank (NAB) – we remain underweight the Australian bank reflecting our negative sector view. The elevated valuations of the Australian banking sector are not reflective of the fundamental outlook, where we expect flat to deteriorating pre-provision profits through declining net interest margins, elevated expense growth and modest loan growth.

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 further challenged 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 its more recently acquired business Vifor (now approximately 15% of group earnings) does provide differentiation, we view the business as lower quality than CSL's core plasma franchise. Considering this operating outlook, we do not regard the current FY24 valuation (30.2 times P/E, 20.9 times EV/EBITDA) as overly attractive at this time, with a preference for ResMed.

Wesfarmers (WES) – we retain an underweight position in the diversified conglomerate. While we believe that WES's core retail businesses (Bunnings/Kmart) will trade well in the current environment (reflecting a flight from the consumer to value), its non-retail exposures (e.g. WesCEF/Lithium) will continue to dilute the quality of the business. With the company still trading on a premium FY25 earnings multiple of 26.3 times vs 18.6 times 10yr average and a 3.3% dividend yield we believe better opportunities can be found elsewhere.

Market outlook

Global equity markets have clearly had a very strong rally from the October lows and, in the first half of calendar year 2024 developed market equities have returned 11.2%. Despite the sharp reappraisal of risk in April our expectations of a bounce back in May and June were realised as investors became less focussed on spillover risks from Gaza and the growth and inflation data both turned more supportive of major economy interest rate reduction.

After the stronger inflation data in 1Q and the sharp shift in interest rate expectations that attended the data, more recent data and communication from the US Federal Reserve supports the bigger picture view that inflation will continue to moderate and the easing cycle for US interest rates is still likely to commence in 2024. Specifically, core-PCE was better behaved than the CPI data and the subsequent data on producer prices, import prices and key labour market measures suggest little threat to the overarching theme that inflation is more likely to moderate than accelerate through the remainder of 2024.

Indeed, interest rate easing commenced with the Swiss National Bank in March, which was followed by Sweden's Riksbank in May and the Bank of Canada and ECB both cutting on June 6. The Bank of England and Norges are also likely to ease in 3Q. We continue to expect the Fed to ease in September and December this year.

Turning to Australia's prospects, a weak finish for economic growth in 2023 – expanding just 0.3%qoq, the start of 2024 was similarly unimpressive, expanding by just 0.1%qoq and 1.1%yoy. This completed four consecutive quarters of contracting GDP per capita, declining 1.3%yoy. Our view that Australia would avoid a technical recession appears to have been met and we continue to suggest that the economy will likely accelerate sequentially through 2024 with the improving global backdrop acting as a tailwind. No one should be disputing that the past 12 months 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. Indeed, 2Q2024 has continued to be a subdued operating environment with retail sales, building approvals and consumer confidence all printing below market expectations. The RBA is caught between a relatively weak economy and persistent wage growth and consumer inflation, nevertheless, the bank should be buoyed by signs that the decline in productivity appears to have passed and wage pressures appear to have peaked. With respect to the latter, the 3.75% increase in awards, compared to the 5.75% in 2023, will help expedite an easing in wage pressures through 2H2024.

Australia, like many of its developed nation peers, also printed above consensus inflation in 1Q. However, we believe the upside surprise in Australia's CPI overstates the real-time price pressures. Much of the upside came via government administered prices, which tend to reflect where inflation was in the prior year rather than current cost pressures, and the prevalence of residual seasonality in inflation pressures at the start of the calendar year. Traded goods prices are trending lower and once administered prices are removed, private sector services prices expanded at a relatively subdued 0.7% qoq in 1Q. We remain of the view that underlying inflation will finish 2024 inside the RBA's target band of 2-3% and the RBA will commence a modest easing cycle for interest rates in 4Q 2024.

Against this moderation in inflationary pressure, we expect economic growth to accelerate sequentially through 2024. We expect the upswing in global industrial production to provide a tailwind for Australian economic growth. Rising capex intentions in concert with investment backlogs should support business investment growth and the consumer outlook should be supported by a recovery in real household income growth driven by ongoing wage growth, income tax cuts, cost of living support delivered in the Budget and the commencement of the rate easing cycle later in 2024.

As a consequence, 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 2.0% v a consensus forecast of 1.4%, bond yields to finish the year at 4.5%, the $A/$US to reach 72c, and Australian equities to return 10% in in large caps and 15% in small caps.

We are most overweight stocks within the Utilities, Industrials and Materials sectors, and are underweight Financials, Consumer Staples and Health Care.

Sector allocation

	Portfolio %	Benchmark %	Active %
Communication Services	5.38	3.57	1.81
Consumer Discretionary	8.01	7.02	0.99
Consumer Staples	0.00	4.00	-4.00
Energy	5.24	4.80	0.44
Financials	19.79	30.22	-10.43
Health Care	6.93	9.70	-2.77
Industrials	9.82	6.82	2.99
Information Technology	5.93	3.11	2.82
Materials	25.48	22.61	2.87
Real Estate	5.13	6.65	-1.52
Utilities	5.88	1.49	4.39

Top 5 holdings

	Portfolio %	Benchmark %	Active %
BHP Group	10.89	9.83	1.06
Commonwealth Bank of Australia	6.50	8.72	-2.22
Woodside Energy	5.24	2.29	2.95
Westpac Banking	5.19	3.96	1.23
Transurban	3.98	1.68	2.29

Key active positions

Overweights	Portfolio %	Benchmark %	Active %
ResMed	3.87	0.81	3.06
Woodside Energy	5.24	2.29	2.95
Reliance Worldwide	2.85	0.17	2.69
Underweights			
National Australia Bank	0.00	4.60	-4.60
CSL	1.43	5.90	-4.47
Wesfarmers	0.00	3.21	-3.21

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	1.43	-5.07	-5.80	-3.36
Distribution return	5.18	11.64	12.89	9.61

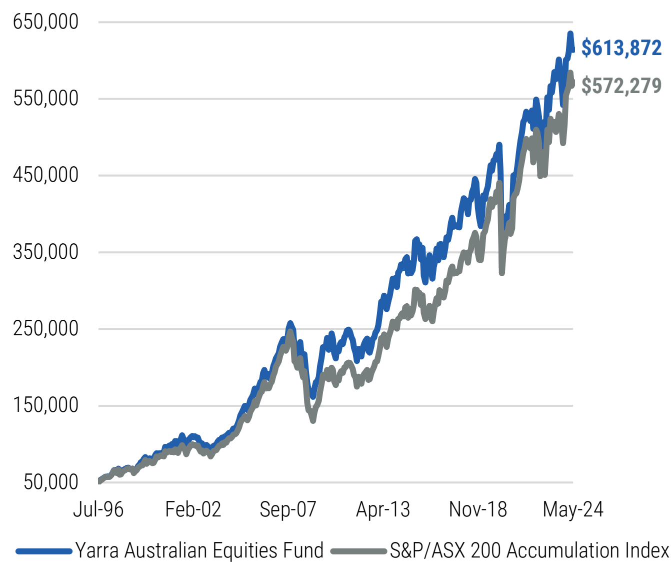
The Growth Return is measured by the movement in the Fund's unit price (inclusive of fees), ex-distribution, and can be positive or negative as the unit price can fluctuate with changes in the underlying market value of the Fund's assets. The Distribution Return is the amount that is paid to unitholders 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$100.4 mn as at 31 May 2024	
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 May 2024.



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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