# Portfolio report

UBS Australian Share Fund
Asia Pacific Equity Indexed
Client report from 01.04.2024 to 30.06.2024

## Performance Comments

After fees and expenses, the Portfolio decreased by 3.60% during the quarter, underperforming its benchmark by 240 bps.

The largest positive contributors were Origin Energy, Fortescue and James Hardie Industries. Origin Energy outperformed during the period trading up as the market factored in the recent uplift in wholesale electricity prices while our underweight position in Fortescue contributed positively as the company underperformed, largely due to the significant decline in iron ore prices. Our underweight position in James Hardie was a source of outperformance as the leading building materials supply company underperformed during the period driven by the release of a disappointing fourth quarter and full year update.

The largest detractors during the period were Reliance Worldwide, NAB and Sims. Reliance Worldwide underperformed as the plumbing supplies company gave back some of its strong CYTD returns during the period as the combination of higher interest rates in the USA and rising copper prices weighed on the share price. Our underweight position in NAB was a headwind despite minimal company specific news while Sims underperformed as the steel producer underperformed following an operational update that disappointed relative to expectations.

| % Return (Net) | Fund[1] | Benchmark* | Difference |
|---|---|---|---|
| 3 months | (3.60) | (1.20) | (2.40) |
| 1 years | 4.91 | 11.92 | (7.01) |
| 3 years | 5.62 | 6.07 | (0.45) |
| 5 years | 6.47 | 7.21 | (0.74) |
| Calendar Year to Date | 2.02 | 4.16 | (2.14) |
| Since inception (07/92) | 9.48 | 9.29 | 0.19 |

[1] Performance figures are net of ongoing fees and expenses.

* S&P/ASX 300 Accumulation Index

The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.

Source: UBS Asset Management. These figures refer to the past. Past performance is not a reliable indicator of future results.

## Stock Contributors & Detractors (%)

| Company name | Return | Contribution | Over / underweight |
|---|---|---|---|
| Origin Energy | 18.04 | 0.44 | OW |
| Fortescue | (16.69) | 0.28 | UW |
| James Hardie Industries | (23.23) | 0.24 | UW |
| Insurance Australia | 11.56 | 0.20 | OW |
| Westpac Banking Corporation | 7.88 | 0.12 | OW |
| **Total of top 5 contributors** | | **1.28** | |
| Worley | (10.57) | (0.24) | OW |
| Vicinity Centres | (13.15) | (0.26) | OW |
| Sims. | (19.03) | (0.34) | OW |
| National Australia Bank | 7.16 | (0.36) | UW |
| Reliance Worldwide Corp. | (21.39) | (0.63) | OW |
| **Total of top 5 detractors** | | **(1.83)** | |

Note: Position at quarter-end, which may be different to the position during the quarter.

## Portfolio Positioning

**Active Positions by Industry Group (%)**

| Top 5 Overweights | | Top 5 Underweights | |
|---|---|---|---|
| Utilities | 4.61 | Banks | (6.53) |
| Capital Goods | 4.43 | Pharmaceuticals, Biotechnology & Life Sciences | (4.74) |
| Media & Entertainment | 4.23 | Financial Services | (4.13) |
| Materials | 3.85 | Equity Real Estate Investment Trusts (Reits) | (3.80) |
| Software & Services | 3.20 | Consumer Staples Distribution & Retail | (3.21) |

**Active Positions by Stock (%)**

| Top 5 Overweights | | Top 5 Underweights | |
|---|---|---|---|
| Woodside Energy | 3.45 | National Australia Bank | (4.66) |
| Worley | 2.98 | CSL | (4.31) |
| Xero | 2.79 | Wesfarmers | (3.07) |
| ResMed | 2.76 | Macquarie | (3.02) |
| CAR | 2.73 | Goodman | (2.49) |

Note: Position at quarter-end, which may be different to the position during the quarter.

## Market Review

The Australian equities market weakened during the second quarter of 2024.

The S&P/ASX 300 Accumulation Index returned -1.2% for the quarter, taking its 12-month return to +11.9%. The S&P/ASX200 fell 1.1% for the quarter. Whilst globally, the MSCI World Index strengthened returning +2.2% for the quarter.

Financials (+4.0%) was the best performing sector despite an increase in the prospect of another rate hike following a higher than anticipated June CPI print. Commonwealth Bank (CBA, +5.9%), Westpac (WBC, +7.9%), and National Australia Bank (NAB, +7.2%) all performing strongly during the period.

By contrast, Materials (-5.9%) was the weakest performing sector with BHP Group (BHP, -3.6%) the main detractor following a decrease in iron ore and copper prices during the quarter. Fortescue (FMG, -16.7%) was also a notable underperformer during the period, also reflecting the weakness in the iron ore price.

Real Estate (-6.0%) was also a negative performing sector as short-term bond yields ticked higher during the quarter. Underperformance stemmed from across the sector as Mirvac Group (MGR, -18.1%), Stockland (SGP, -10.6%) and Charter Hall Group (CHC, -17.1%) were the main detractors during the quarter.

## Outlook & Strategy

The 2023-24 financial year is now complete and concludes what we have broadly labelled the "hope" phase for financial markets – an environment where equities rally via PE expansion rather than via earnings growth. It's now time for the individual stocks to deliver on those growth expectations, which typically is a bumpier experience for markets. In broad terms, it was a good financial year for markets. A 20% return for global equity markets, regardless of whether you bothered to hedge or not, was only just eclipsed by a 21% return from gold, thanks in part to central bank buying. REITs returned a solid 17%, commodities rose a respectable 15%, and although it was a weaker finish to the financial year the AS200 returned an above average 12% - the same return generated by alternative assets. In contrast, Australian fixed interest returned 3.7% and global bonds a paltry 0.9%.

We adopted a top-down pro-risk stance heading into Q4 2023, in part because we expected consensus to lift their economic growth forecasts, lower their inflation forecasts and for interest rates to commence declining across the major economies from mid-2024. Interest rate reductions in Sweden, Switzerland, Canada and the Euro Area are likely to be met with the Bank of England likely easing in August and we believe the Fed will commence its easing cycle in September. All of this is good news, however, there is now less of a gap between our long held more optimist views on global growth and the consensus. There are also signs that the positive momentum for global economic growth is starting to falter. Broadly, we think most of the good news we have been flagging is now largely imbedded in market pricing and we are somewhat uncomfortable with the narrow nature of the equity rally and what promises to be a drawn out and we think ultimately demoralising US election campaign. In short, we are expecting that transitioning from the more thematic driven "hope" phase of the cycle to the more stock specific mid-cycle phase for financial markets will not come without some growing pains in Q3 2024.

Turning to Australia, a recession has been avoided, yet Australia continues to operate near stall speed. GDP increased just 0.1%qoq taking the annual rate to 1.1%yoy. Excluding COVID this is the slowest annual rate of growth in 32 years. GDP per capita declined 0.4%qoq – the 4th consecutive decline - taking the annual rate to negative 1.3%yoy. This is the worst contraction since December quarter 1991 excluding the COVID period, and this measure has only expanded once in the past 7 quarters. No one should be disputing that the past 12 months likely felt like a recession for many Australians.

The Reserve Bank of Australia (RBA) is caught between a relatively weak economy and persistent wage growth and consumer inflation, nevertheless, the RBA 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 and the volatile monthly CPI measure points to high and persistent inflation in 2Q. 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 are expanding at an inflation target consistent pace. While we can't rule out the RBA choosing to hike again in August, we remain of the view that 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, albeit remaining well below 'potential' growth. 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 constructive on the outlook for the Australian economy and the equity market outlook for 2024-25, even if there are some nearer term headwinds. We expect economic growth to average 1.75% v a consensus forecast of 1.3% in 2024, bond yields to finish the year at 4.5%, the $A/$US to reach 72c, and Australian equities to return 10%.

We are overweight the Utilities, Industrials and Information Technology sectors, and are underweight Financials, Consumer Staples, and Health Care.

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