

Australian Equities

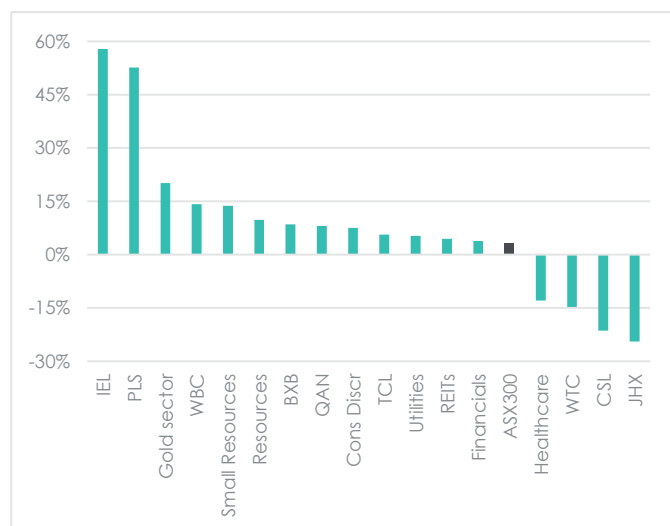
Reporting Season Review

This report aims to give readers an overview of the recent Australian reporting season. As the Aussie market continues to record new highs and new record earnings multiples, signs of excess are evident in certain sectors. We remain focused on companies with competitive advantage, buy at reasonable valuations, and diversify across sectors. We believe a portfolio built in this way should deliver resilient long-term outperformance.

What happened in August

Investors reacted with enthusiasm to the August reporting season, pushing the S&P ASX300 index up 3.2% in the month. The best sector performer was Resources up +9.8%, within which Small Resources was +13.7% and Gold +20.1%, a move that seemed to have nothing to do with results or even with commodity prices, which were subdued in the month. Outside of resources, the best sectors were Consumer Discretionary +7.5%, Utilities +5.3%, REITs +4.5% and Financials +3.8%. The big laggard was Healthcare -12.9% along with Information Technology -1.4%.

Chart 1: Performance through August 2025 of mentioned companies and sectors. (Source: FactSet, IRESS)



Key takeaways from Reporting Season

Australia is faring better than the US...

Companies with strong exposure to the Australian economy generally performed well this reporting season, with solid results from names like JB Hi-Fi, Qantas, and Virgin Australia. We think Jetstar CEO Stephanie Tully put it lightly when she said, "Australians love to travel". In contrast, businesses with greater reliance on the US economy - such as Brambles, Amcor, James Hardie, and Worley - have reported softer trading conditions in recent months.

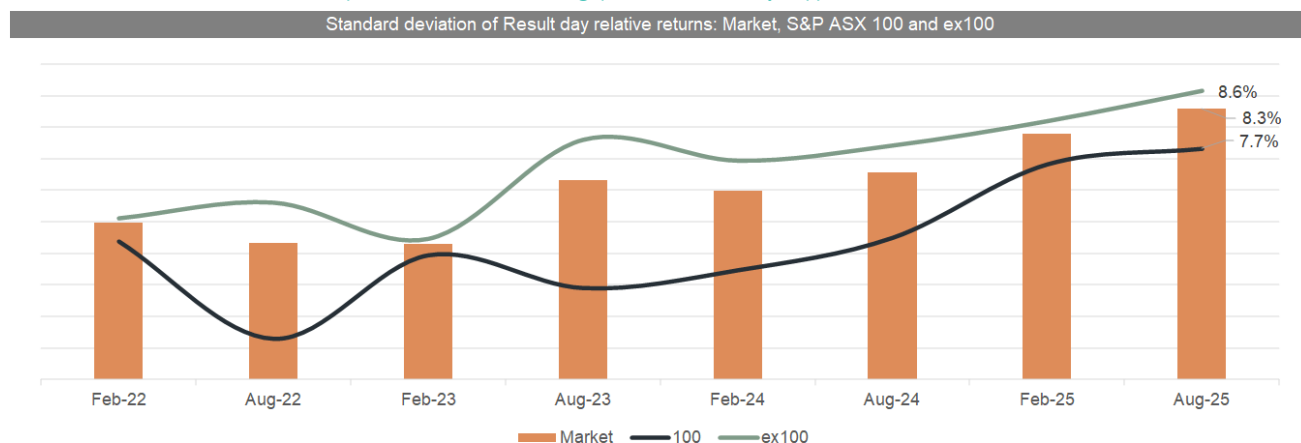
Except if you're in Victoria...

Several businesses commented on challenging conditions in Victoria. Companies described everything from weak trading conditions (e.g. Coates Hire revenue -19%), to work-from-home stifling innovation at CSL, to high levels of theft (e.g. organised crime targeting Rebel Sport stores; thieves targeting the meat departments of Coles to then resell to restaurants and cafes, illegal tobacco decimating legal sales). Traffic on Melbourne toll roads has not returned to pre-pandemic levels, while Transurban said traffic in Brisbane is nearly 20% higher. Wesfarmers said the only area where they are seeing strong growth in Victoria is the sale of home security products within Bunnings!

Volatility was high...

Market reactions to company results have become increasingly volatile, with an intense focus on short-term trading conditions (e.g. retail trading updates for the first 7 weeks of FY26). The rising prevalence of passive investment has likely contributed to lower liquidity, while greater use of algorithmic trading is amplifying the impact of quantitative signals. This may be contributing to some of the valuation anomalies we see in the market; for example, Wesfarmers trading on 37x earnings.

Chart 2: Relative return volatility has been increasing (Source: Barrenjoey)



And its AI or nowhere...

The AI thematic continues to attract both extreme enthusiasm and puzzling share price reactions - for example, Megaport's FY26/27 earnings were cut by 200%/120% due to materially higher reinvestment, yet the stock shot up 15% since reporting to the end of August! MP1 CEO Michael Reid did say "there is no one close to what we can do on the planet" though. So far, AI hasn't delivered clear cost savings or productivity gains for Australian firms; CBA even had to reverse plans to cut 45 call-centre jobs after its new 'voicebot' drove call volumes unmanageably higher.

For some of our key portfolio holdings, we were pleased to see business improvement and better capital efficiency. Improving return on capital is an important driver of long-term shareholder returns.

- Qantas (+8%) is demonstrating higher profitability from investment in new fleet,
- Brambles (+9%) is improving the efficiency of its pallet pool through investment in data, and
- Transurban (+6%) is being more disciplined with capital and operating costs, boosting the outlook for distributions.

Other notable results:

- CSL Ltd (owned, -21%) fell on a weaker outlook for revenue growth than the market had been expecting. It looks like competitors may have gained ground in the core IG market, which would be an important development. We think the stock looks cheap, but we have not added to our position pending further clarity on the competitive position.
- James Hardie (owned, -25%) fell on lower revenue and margin. Reduced disclosure post the Azek deal has added to market confusion and raised questions about market share trends. This is a small position for us now, after trimming aggressively post the Azek deal.
- IDP Education (owned, +58%) rose after providing a more positive outlook than the market had expected. The strong cash flow in the FY25 result removes any lingering concern around the balance sheet. FY26 will feature cost reductions that should position IEL to benefit from future recovery in student numbers. The stock still looks cheap to us.

- Westpac Bank (not owned, +14%) rose on a quarterly update. Profit trends were strong in the quarter, but we'd be cautious of extrapolating a 12-week period because revenue can be volatile from quarter to quarter. WBC looks expensive on a record PE multiple of 20x. CBA reported a full-year result in line with expectations, but the stock fell 3% due to its extremely elevated valuation.
- Wisetech (not owned, -15%) fell on slowing revenue growth in its core business. Operating trends are mostly obscured by a large acquisition, but underlying growth appears to be heavily driven by price. We are surprised at the lack of scrutiny this company seems to attract, as deadlines for proposed company-transforming product releases continue to slip.
- Lithium stocks were standout performers (Pilbara Minerals, not owned, +50%) as spodumene prices surged 50% over the past three months, fuelled by compliance reviews in China. However, we remain cautious on the sustainability of this rally, with Australia's idle supply ready to re-enter the market and potentially cap prices going forward.

The main drivers of relative performance during the month were big moves in the gold and REIT sectors, which had nothing to do with company results. These sectors have the largest passive shareholdings and can be driven by flows. For example, the gold sector rallied 20% in the month while the gold price only increased by 2%.

Outlook

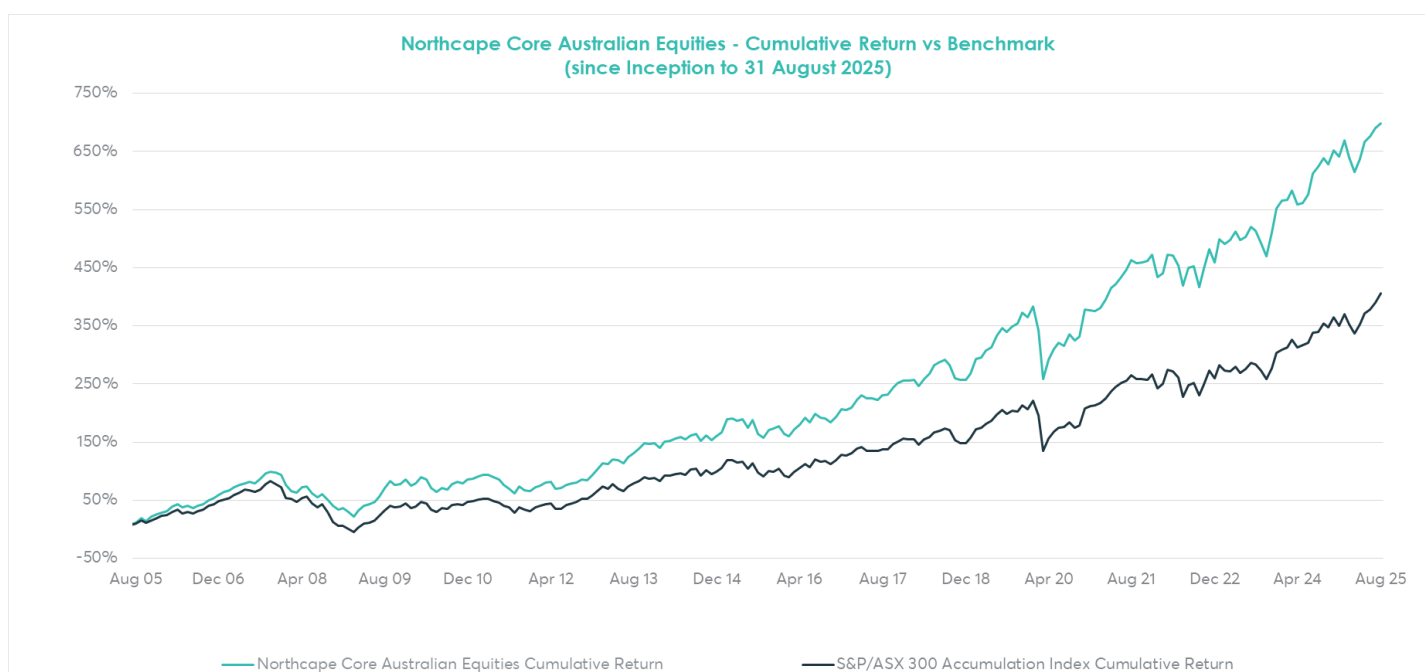
As the market continues to record new highs and new record earnings multiples, signs of excess are evident in certain sectors including technology and banks, and speculative flows are driving moves in commodity producers. While missing out on some of these late-stage rallies can be painful, the best long-term returns don't come from chasing the hottest sectors with no regard for valuation. Our longstanding approach is to focus on companies with competitive advantage, buy at reasonable valuations, and diversify across sectors. A portfolio built in this way should outperform the market over the long term and be more resilient during market downturns.

Northcape overview:

Northcape is a boutique investment manager wholly owned by staff. We specialise in managing concentrated equity portfolios with a quality bias across Australian and Emerging Markets equities. Northcape manages over A\$15 billion of investment capital on behalf of a range of global investors. We have a proud track record of achieving strong outperformance since our inception in 2004.

Australian Equity Fund:

The Core Australian Equity Fund is a high-conviction portfolio of quality Australian companies with a 20-year track record of outperformance. Fundamental investment research is focused on identifying businesses with sound balance sheets, strong management, above average growth prospects, high returns on equity and a meaningful competitive advantage. We are patient investors with a long-term investment horizon. The outcome is a low-turnover portfolio of carefully selected businesses that delivers resilient and sustained performance for clients.

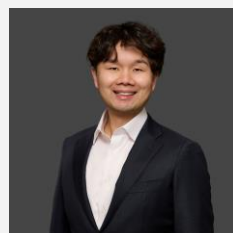


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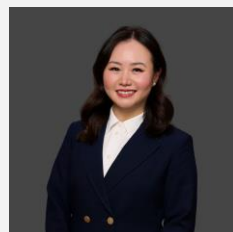
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