

2026: A Turning Point for Australian Equities?

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2025: Another solid year for equities

Notwithstanding the late CY25 share market pullback – ASX 200 -3.0% over the three months ending 30 Nov – investors appear set to close out the year in positive territory.

Gains have again been healthy, with trailing 12-month domestic equity returns at +5.5% with one month to play in the year, albeit modestly below the ASX 200's 3-year (+9.7%), 5-year (+9.9%) and 10-year total returns (+9.5%).

However, not all “sector boats” have risen evenly. Substantial sector divergence has been a feature of the last 12-months.

Specifically:

- Resources (25% of ASX) rallied hard (+23.6%), supported by commodity price strength (USD) from copper (+24%), iron ore (+1%) and gold (+60%);
- Banks (24% of ASX) performed modestly ahead of market (+6.5%), supported by modest earnings growth and ongoing margin expansion (sector now trades at 19-times forward earnings, which is 40% above the 20-year average); and
- Industrials (35% of ASX) underperformed relatively (+0.8%), with key sectors Technology (-15%) and Healthcare (-19%) both large detractors, impacted by softening earnings growth relative to prior years.

A ‘side-ways’ economic outlook highlights the power of companies that can win based on ‘micro’ circumstances (rather than relying on ‘macro’ help)

With input from our in-house macro-economic team, we see a macro-outlook moving into CY26 of improving private demand, but with monetary policy support being limited as fiscal support peaks:

- Economic growth in Australia has improved (GDP +2.1% (y/y) as of Q3, +0.4% (y/y) on per capita basis) but remains well below ‘potential’ growth of ~2.7%;
- An extraordinary set of ‘own goals’ weigh on confidence and growth. Drivers range from lack of cohesive energy policies, industrial relations missteps to elevated government expenditure; and
- The global economic environment is unlikely to help short-term, with China’s trajectory longer-term now clearly challenged.

In this environment we would anticipate that those companies with attractive quality characteristics stemming from defensible market share positions and ability to offset increased input cost pressures will be better placed to outperform in the period ahead.

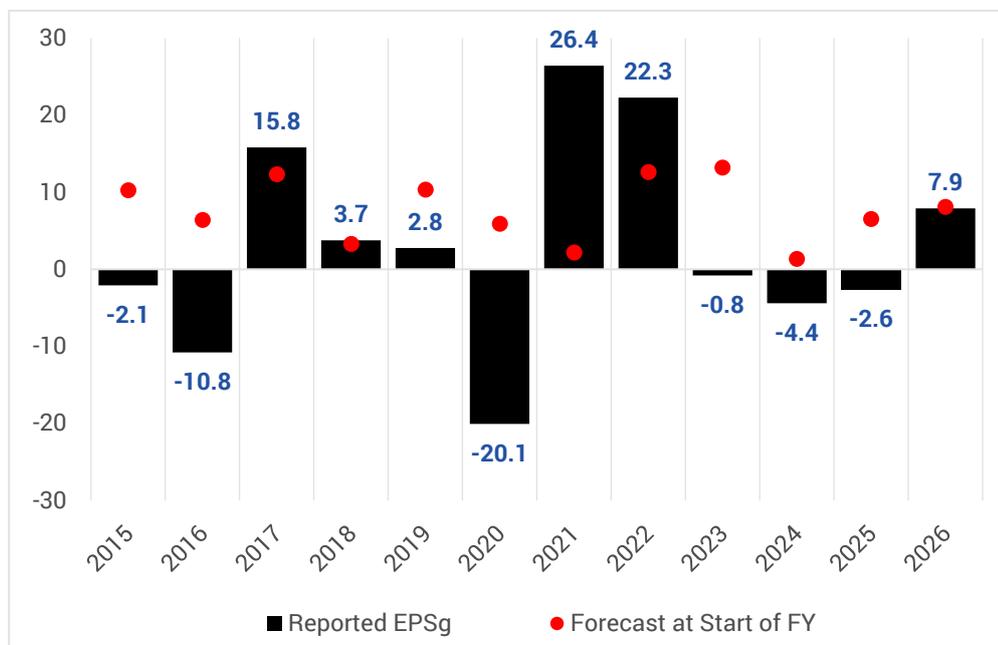


2026: A return of EPS growth after three-years of declines

Improving earnings into FY26 is one of the key drivers of optimism for the ASX 200 as we head into CY26.

Consensus now expects ASX 200 earnings growth of +7.9% in FY26 (refer Chart 1), bouncing back from three successive years of earnings declines over FY23-25 following the COVID recovery years FY21-22.

Chart 1. A return to positive ASX 200 earnings growth expected in FY2026



Source: Goldman Sachs Research/YCM, Dec 2025.

Importantly, we expect all major sectors to contribute to positive earnings growth, with consensus forecasting Banks to grow earnings at +4.8% and Resources at +11.4% (refer Figure 1). Importantly, this +7.9% expected market earnings growth has accelerated from the +3.7% as at the end of the last reporting season (only five months ago), driven by ongoing improvement in the health of the consumer and commodity price expectations, and strengthening earnings growth for the Banking and Resources sectors.

Figure 1. Divergent sector contribution to consensus ASX 200 EPS growth

	Index Weight (%)	EPS growth (%)			Change, % (5-mths)
		FY25	FY26	FY27	FY26
ASX 200	100	-2.7	+7.9	+7.7	+4.2
Industrials	35	+1.1	+9.4	+12.7	-1.1
Banks	24	+6.8	+4.8	+3.7	+3.8
Resources	25	-13.2	+11.4	+7.2	+11.0
Healthcare	8	+12.8	+10.0	+12.4	-1.0

Source: Goldman Sachs Research/YCM, Dec 2025.

Remaining highly selective around Industrials (35% of ASX 200)

Outside of the resources sector, we expect Industrials to be the next key driver of earnings growth for equities in FY26, particularly from the Consumer Staples, Discretionary Retail and Telecommunication sectors.

This said, we believe a highly selective approach is warranted intra-sector, with evidence of pricing fatigue setting in across many industries (volume decay, trading down etc). This was clear in the August reporting season which showed further normalization in Industrial EBITDA margins to 17.6% (vs. 17.8% pcp).

Importantly, these EBITDA margins (Industrials) remain 110 bps above pre-COVID levels and a vulnerability for some companies without the market position, value proposition, and/or product differentiation to offset persistent input cost inflation. Margin pressures are building, not abating.

In the context of Industrials trading at average P/E multiples +23% above long-run averages (refer Figure 2), we put a heavier emphasis on earnings sustainability in stock selection.

Transurban, for example, is one industrial company we see as attractive in this otherwise 'expensive' sector.

Figure 2. ASX 200 valuation metrics vs 20-year long-run average

PE NTM	ASX 200	Industrials	Banks	Resources	Healthcare
Current	17.9	23.2	18.7	14.0	22.5
20-year Average	14.7	18.8	13.3	13.3	24.4
Premium/(Discount)	+22%	+23%	+40%	+6%	-8%

Source: Goldman Sachs Research/YCM, Dec 2025.

Early signs indicate an unwind in banks and overheated names

From a fundamental perspective, we expect cyclical pressures to be modest for the banks, and we are not concerned about a mortgage 'bust' or an extreme bad debt cycle. Key challenges into the medium term remain centred around cost escalation, intense competition, and maturity. Stock valuations remain at elevated levels creating vulnerability, with the sector trading at a 40% P/E multiple premium to historical averages (Figure 2).

Early signs indicating an unwind are here, with the banks declining 5% over the past three-months, and CBA falling by 13% over the month of November alone. **Wesfarmers**, also viewed as a large cap bellwether, has fallen more than 10% from recent peak levels despite an absence of any 'new' news.

We expect significant Resources divergence

Our research suggests that the Resources sector no longer moves in lockstep with China and that China's growth potential in the medium-term is dramatically lower (aging population, escalating debt, infrastructure build out reaching maturity). As a result, supply (or lack there-of) becomes a more significant factor of commodity research.

Bulk commodities appear more vulnerable (iron ore has decoupled from fundamentals and has medium-term headwinds), while base metals (in particular copper) fail to reflect a cyclical rebound, upside from electrification demand or supply-related challenges.

For us, stock rather than sector opportunities are key for the period ahead.

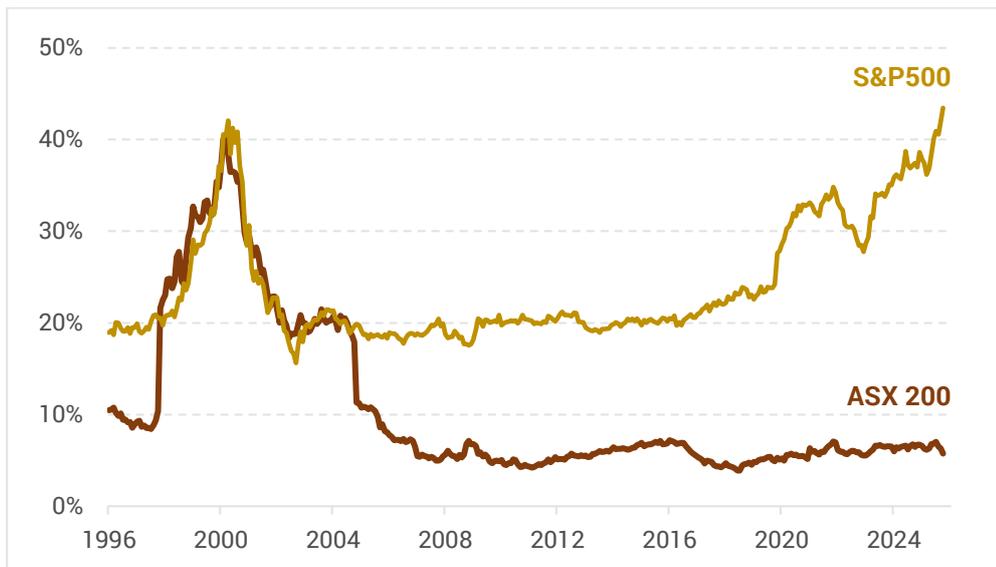
We expect the environment will support copper exposed names such as **Sandfire Resources** and **Capstone Copper**, and oil & gas leader **Woodside**, with a favourable backdrop for gas/LNG demand.

A number of factors support ASX 200 resilience in the event of 'AI downturn'

Debate persists around whether pockets of investment markets have over or underpriced the potential future impact from AI.

To the degree that any 'unwind' would likely impact sectors beyond just technology such as media and telecommunications (as it did in the dot-com bust of 2000, refer Chart 2) it is notable that right now only around 6% of the ASX 200 market cap is 'tech exposed,' well below the level in the USA today (~43%), and indeed on the ASX 200 back in 2000. To this end, we can expect more resilience from the Australian equity market should perceptions – and reality – change around 'AI' beneficiaries.

Chart 2. 'Tech exposures' (Technology, Media, and Telecommunications sector weight)

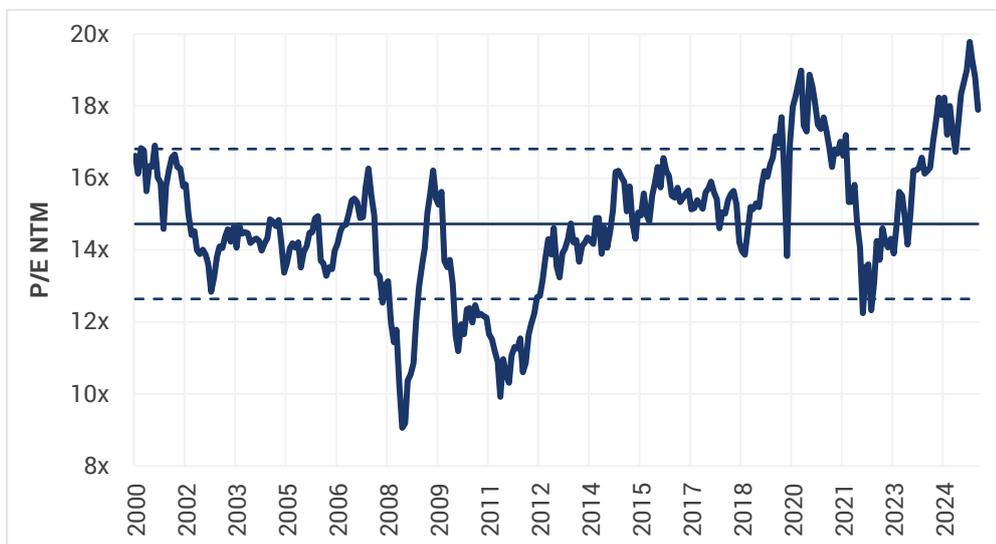


Source: UBS Research/YCM, Dec 2025.

Valuations are above long-term averages, but bargains still exist

From a top-down perspective, ASX 200 companies in aggregate are trading at elevated levels given a forward P/E of 17.9-times, which is 22% above the 20-yr average (Chart 3).

Chart 3. ASX 200 PER, NTM



Source: Goldman Sachs Research/YCM, Dec 2025.

2026: Focusing on identifiable catalysts

Looking ahead, our selective approach highlights several themes that we believe could leave a number of large-cap stocks well placed to outperform:

- Cyclical rebounds – **Mirvac** (Housing), **Nine Entertainment** (Media), **Woodside** (Energy)
- Business turnarounds – **TPG** (Mobile Telecom), **Ramsay Healthcare** (Hospitals)
- Underestimated growth stocks – **NextDC** (Datacentres), **ResMed** (Healthcare Devices)

Conviction positions away from the benchmark and with identifiable catalysts give us confidence in our ability to outperform over 2026.

Importantly, risk management is at the forefront of our investment approach ensuring that stock ideas are weighted appropriately based on risk/reward, ensuring balanced portfolios which can outperform through varied market cycles.

Stemming from our proactive and bottom-up research approach, our 16-person equities team conducts more than 2,500 meetings annually which underpins a strong pipeline of new ideas for the year ahead.



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