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REPORTING SEASON WRAP

LOW HURDLE JUMPED

The reporting season gets a pass mark. FY24 results have, on average, met low earnings expectations, with the ASX 200 industrials navigating a challenging macro environment.

Margins the swing factor

FY24 reporting season highlighted the importance of margin management. Revenue beats were less prominent than earnings beats, indicating that margins have been the key story of beats this reporting season through cost control/efficiencies/pricing. The contrast between fewer revenue misses to earnings misses indicates that a lack of margin control was also a key reason for EPS misses this reporting season.

For the ASX 200 Industrials, the % of beats and misses were broadly even (28% vs 27% of total results, respectively), with a significant proportion of results in line (+/-2%) with consensus (45%).

Misses punished

Companies that missed expectations experienced sharp price declines (on average). While exceeding expectations was rewarded, the magnitude of these gains was smaller in comparison to the penalties for misses.

Elevated P/E ratios indicated lofty market expectations going into reporting season. Therefore, it is unsurprising that when results did not meet expectations, share prices were punished.

FY25 earnings downgraded

FY25/FY26 consensus earnings continued to be downgraded in reporting season as guidance/outlook/trading statements have, on aggregate, underwhelmed the market. ASX 200 FY25 EPS was downgraded by 1.3% in August, and FY25 earnings growth is now expected to be ~3.7% vs ~5.4% pre-reporting season.

Downgrades have outweighed upgrades this reporting season. 63% of the ASX 200 industrials (that reported) were downgraded and 68% of the ASX 200 resources were downgraded in August.

Earnings downgrades at a sector level have been broad, with only financials coming out of reporting season with more upgrades than downgrades. Tech has seen upgrades on an aggregate basis with a great result from large cap WiseTech (WTC).

Reporting Season Themes

- **Margin management**
  The ability to manage margins effectively was crucial, with companies focusing on cost control and operational efficiencies to protect their bottom line.
- **Tech shines**
  The technology sector emerged as a reporting season winner, with several companies reporting strong financial results.
- **Bank margins stabilising**
  Banks showed signs of improvement, with net interest margins stabilising and competitive pressures easing.
- **Supermarket sweep**
  Coles (COL) outperformed Woolworths (WOW), driven by improved in-store execution, effective campaigns, and online growth.
- **Consumer discretionary divergence**
  The consumer discretionary sector experienced mixed results, with some retailers demonstrating resilience while others struggled with slowing consumer spending and rising costs.
- **Residential developers' bifurcation**
  The residential development sector also showed a mixed performance, with some developers facing challenges while others showed signs of resilience.
- **Healthcare keeps growing**
  The healthcare sector presented a mixed picture, with some companies facing downgrades (CSL/COH), and others delivered strong results (RMD). The sector's overall outlook remains positive, with continued growth expected.

Our view – Market to look across the valley

The reporting season has not raised a significant red flag. While FY24 earnings growth has declined and FY25 is expected to be sluggish, the situation is not dire.

In line with our expectations, FY25 earnings estimates were revised downwards this reporting season. The initial projection of ~5% earnings growth was overly optimistic considering the prevailing high-interest rate environment and economic slowdown that is set to continue for the next 6 months.

Currently, the market seems to be looking beyond the near-term challenges, instead focusing on FY26 (or 2H25), when interest rate cuts are expected to take full effect, thereby stimulating earnings growth.

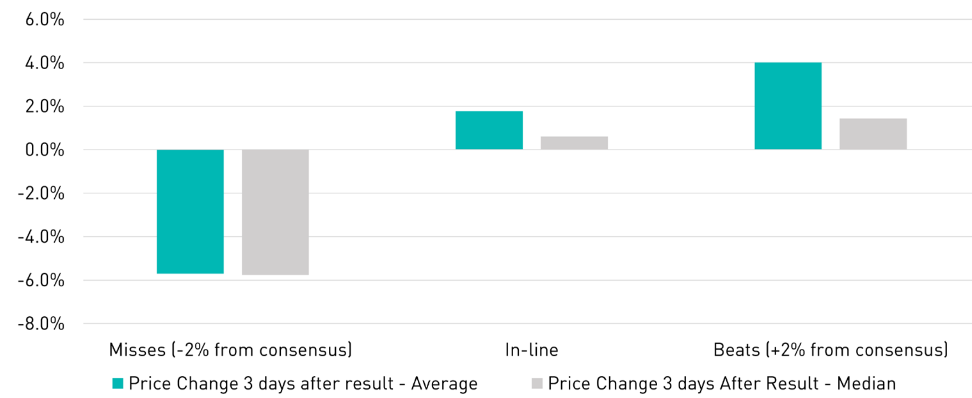
James Hardie's (JHX) stock performance serves as a prime example of this forward-looking market sentiment. Despite an initial sell-off of 2.9% on the day of its earnings release (on soft 2Q25 guidance), the stock has subsequently surged 15%, fuelled by hopes of US rate cuts in September (JHX is ~80% North American focused).

Therefore, while the coming 6-12 months may be tough for earnings, we believe the market will weather this period of earnings volatility, keeping its sights set on the anticipated FY26 recovery.

Figure 1 ASX 200 Industrial companies were broadly even for beats vs misses in reporting season

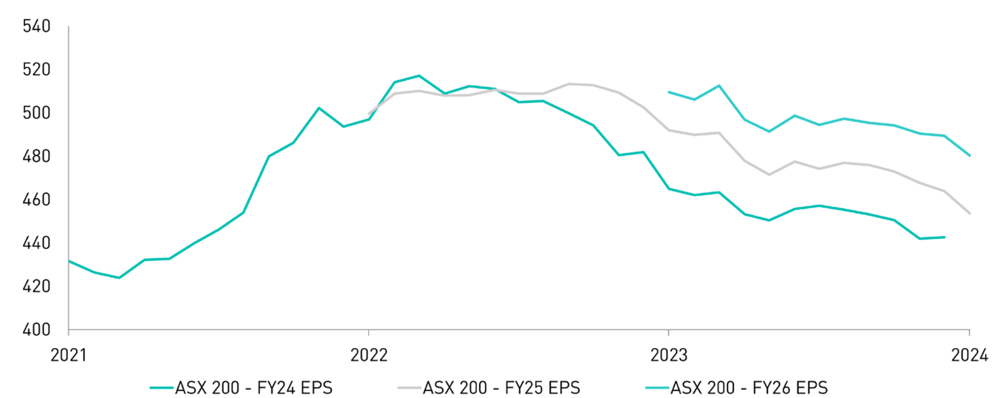
Source: Refinitiv, Visible Alpha, Bell Potter

Figure 2 ASX 200 Industrials earnings misses were punished more by the market than beats were supported



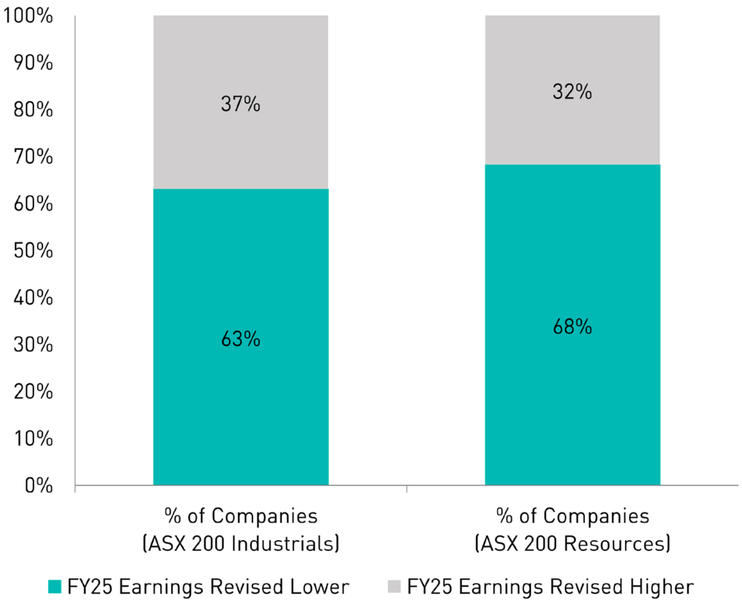
Source: Refinitiv, Bell Potter

Figure 3 ASX 200 FY25/FY26 earnings were revised down over reporting season



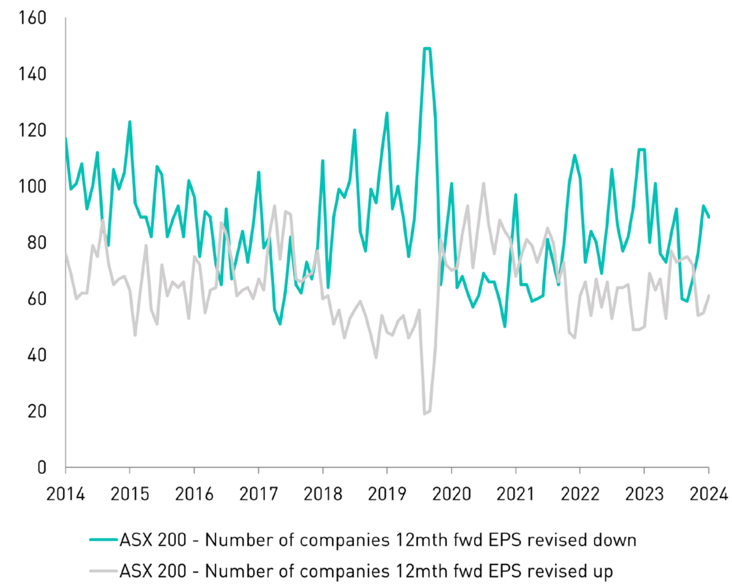
Source: Refinitiv

Figure 4 More companies had earnings revised lower than higher



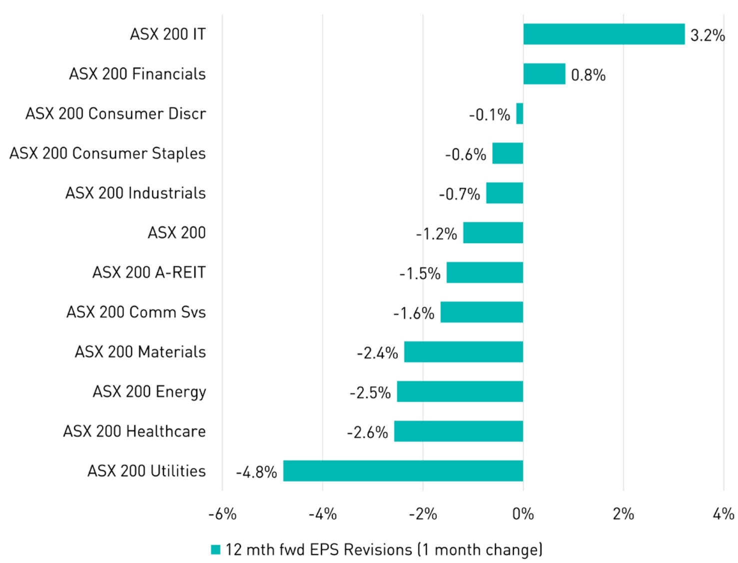
Source: Refinitiv

Figure 5 More companies downgrading than upgrading is common, so not a significant concern for the market



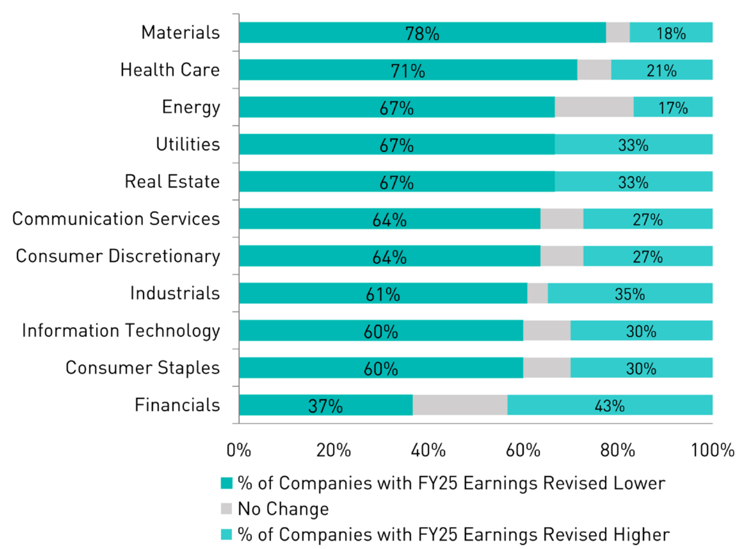
Source: Refinitiv

Figure 6 Tech and financials are the only sectors with upgrades at the sector level



Source: Refinitiv

Figure 7 Earnings downgrades have been broad



Source: Refinitiv, Bell Potter

KEY THEMES OF REPORTING SEASON

1. Margin management

Quality companies, demonstrating their resilience and adaptability in a challenging economic climate, strategically managed costs and operational efficiencies to protect their bottom line. Additionally, some leveraged their strong brand reputation and market position to implement strategic price increases, improving margins.

Brambles (BXB)	Strong pricing, asset productivity improvements, and operating leverage drove a strong result even with flat volumes.
James Hardie (JHX)	Used pricing power to offset flat volumes, exceeding market expectations for 1Q25 earnings.
JB Hi-Fi (JBH)	Lower discounting and effective cost management supported GM and EBIT margins. This is one of the best results of reporting season.

Companies hit by cyclical weakness but couldn't manage margins have seen some of the worst downgrades in reporting season.

Seek (SEK)	Lower revenue from lower job ad volumes was compounded by higher opex leading to a 14% fall in FY24 EBITDA, after a margin contraction of 4 percentage points to 43%. FY25 earnings have been downgraded by ~30% in August.
Tabcorp (TAH)	Lower revenue from a soft/competitive wagering market and cost inflation drove EBITDA down ~19%. FY25 earnings were downgraded 54% in August.

Cyclical pressures will continue in 1H25 (at least), but margin management may have peaked this reporting season.

The necessity of cost control persists, yet the potential for companies to surpass expectations solely through cost-cutting measures in FY25 appears limited. The peak of cost management efforts likely occurred in the first half of 2024.

The retail sector has seen a return to pre-COVID levels of discounting, suggesting that the normalisation process is nearing completion.

Volumes should improve for many cyclical stocks in FY25 (more likely 2H25). However, we are wary of companies that have yet to demonstrate quality in this challenging period, especially those on elevated multiples.

2. Tech strength

The technology sector has demonstrated notable success during the recent reporting season, with several companies reporting strong financial results. WiseTech (WTC), REA Group (REA), and Pro Medicus (PME) have particularly distinguished themselves with their exceptional performances.

WiseTech (WTC)	The company exceeded its guidance range for FY24 EBITDA, primarily due to a better-than-anticipated EBITDA margin. The robust growth in recurring revenue, coupled with customer acquisition and strategic M&A activity related to CargoWise, significantly contributed to its earnings. WiseTech also implemented price increases to counter inflation and executed a company-wide cost-efficiency program, resulting in substantial cost savings.
REA Group (REA)	The company witnessed a remarkable 27% increase in EBITDA, fueled by growth in residential listings, particularly in Sydney and Melbourne. The implementation of double-digit price rises across Commercial & Development further bolstered profitability. Additionally, higher-than-expected revenues from media operations and financial services played a crucial role in driving earnings growth.
Pro Medicus (PME)	While still maintaining a high growth rate of 29%, the company experienced a slight decrease in revenue growth compared to previous years. However, this was more than offset by a notable 1.8% expansion in margins. The company's competitive advantage stems from the shortage of radiologists in the US and the speed and efficiency of its products. The strong adoption of Visage in university hospitals, coupled with contract wins and rapid deployment to new clients, were the primary drivers of Pro Medicus' profitability.

3. Bank margins stabilising

The banks are showing promising signs of margin improvement. CBA's (CBA) and Westpac's (WBC) net interest margins look to be stabilising as competitive pressures within the mortgage market start to ease. This development has led to minor upward revisions in bank earnings forecasts.

While credit quality deteriorated in FY24 due to elevated interest rates, the banks are well provisioned, albeit bad debts are likely to rise in FY25.

The banking sector has delivered solid results, but the outlook for major banks' earnings remains subdued due to the expectation of only moderate growth in the future. The results in August did not change our view that the banks are still too expensive (especially CBA).

4. Supermarket sweep

Coles (COL) is gaining market share from Woolworths (WOW). COL's success can be attributed to a combination of factors, including enhanced in-store execution, impactful value campaigns, and a growing online presence.

While the broader supermarket industry is faces challenges such as moderating food price inflation, cost-conscious consumer behaviour, and intense competition, COL's had a strong result from taking market share.

COL looks more attractive than WOW due to its relatively lower valuation (21x fwd P/E vs 24x) and stronger projected earnings growth (15% vs 9% in FY26). This positive outlook for COL is supported by its ongoing market share gains and the anticipated margin benefits resulting from the implementation of new automated distribution centres and lower levels of in-store theft.

5. Consumer discretionary divergence

The consumer discretionary sector presented an inconsistent narrative. While quality retailers like JB Hi-Fi (JBH) and Super Retail Group (SUL) showcased their resilience through robust earnings and optimistic trading updates, underpinned by astute cost management strategies, a considerable portion of the sector grappled with the dual headwinds of a slowing consumer and escalating costs.

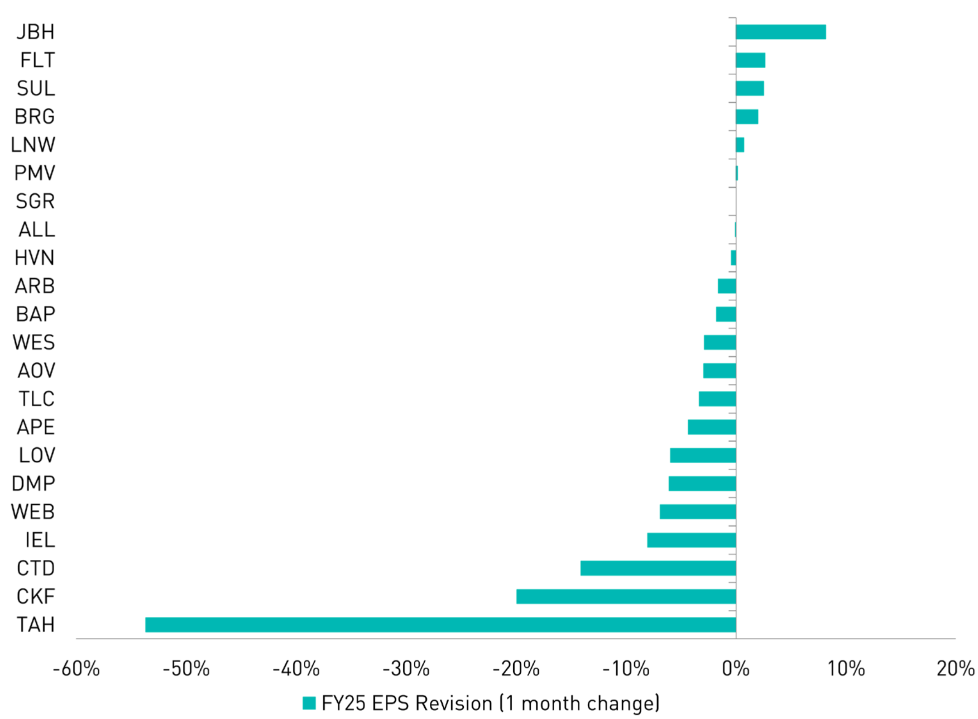
Rising interest rates and inflation have squeezed other pockets of discretionary spending, making it harder for certain retailers and other consumer-focused businesses to maintain sales growth. Additionally, increasing operational costs have put pressure on margins and led to lower profitability without appropriate cost management.

Can the consumer recovery in FY25?

We anticipate a recovery in consumer spending towards the latter part of FY25. Households will have more disposable income due to anticipated interest rate and tax cuts. Real wages are also improving as inflation cools, further strengthening consumers purchasing power.

Retailers can expect significant relief on the cost front in FY25. With a smaller minimum wage increase (+3.75%) compared to FY24 (5.75%) and other inflationary pressures, like rent and electricity costs, expected to moderate or continue moderating, the business environment is set to improve in FY25.

Figure 8 Consumer discretionary earnings revisions are uneven



Source: Refinitiv

6. Residential developers' bifurcation

The residential development sector is currently experiencing a mixed performance, with some developers facing significant challenges while others are showing signs of resilience.

Mirvac (MGR) (NEGATIVE)	MGR's earnings guidance for FY25 was ~11% lower than what analysts were expecting. The miss appears to be primarily due to reduced operating profit margins in their residential business,and higher than expected interest costs.
Lifestyle Communities (LIC) (NEGATIVE)	Low consumer confidence, inflation and interest rates have put pressure on the Victorian property market. Operating profit declined ~26% due to lower new home settlements and increased costs of marketing new projects. LIC's FY25 earnings have been downgraded 21% in August.
Stockland (SGP) (POSITIVE)	SGP had a good result. A key positive from SGP's results was the quarter-over-quarter improvement in residential sales going into the fourth quarter of 2024 and the second half of 2024. Sales in the 4Q were higher despite a decline in inquiries, indicating improved sales conversion and an improving sales environment.

7. Healthcare keeps growing

The healthcare sector presented a mixed bag of results. The sector's overall earnings were downgraded, primarily driven by major index constituents CSL (CSL) and Cochlear (COH) performance.

CSL's results were impacted by weakness in its Vifor and Seqirus segments, which overshadowed the positive underlying gross margin trends in its Behring segment.

COH's results and guidance also fell short of expectations, leading to downgrades for FY25 due to gross margin headwinds and increased R&D expenditure.

However, amidst these challenges, there were also brighter spots in the sector. Resmed (RMD) delivered a strong performance, with robust top-line growth and significant margin expansion driven by a favourable mix shift towards higher-margin mask and software sales. The company's gross margin guidance also surpassed consensus estimates.

Despite the mixed results relative to expectations, the healthcare sector demonstrated impressive above-market earnings growth in FY24, and this trend is projected to continue in the medium term. We maintain a positive outlook on the sector, and still have a preference to CSL, which has strong medium-term earnings growth (+15% pa (FY25-27) at a reasonable valuation (fwd P/E ~29x).

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