



Auscap Newsletter

APRIL 2026

AUSCAP ASSET MANAGEMENT LIMITED

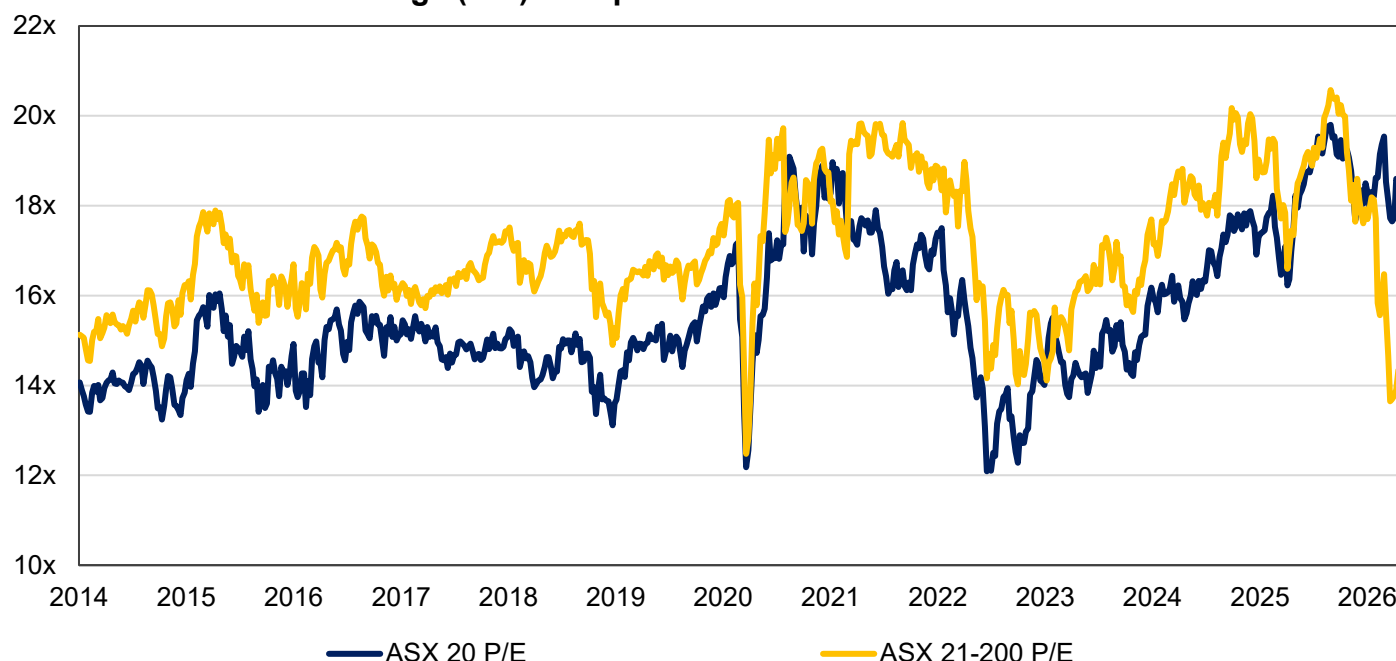
Accepting the risks and buying the best when quality is on sale

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Markets have a strong tendency to swing from one extreme to another. As Howard Marks has often commented, the pendulum of market sentiment swings from greed to fear spending very little time at fair value. Following strong equities market returns in recent years a confluence of events, including primarily developments in artificial intelligence and conflict in the Middle East, has led to a repricing of many securities in recent months, particularly in mid and small capitalisation companies. The mood has changed from optimism to extreme pessimism and this is being reflected in valuations. The question is whether, thinking objectively and behaving rationally in the face of the new information, this is creating opportunities for the patient investor.

The market has certainly become bifurcated in recent months. The larger companies in the domestic market have been less price sensitive to recent developments than the rest of the Australian sharemarket. The 10 largest companies in the ASX200 by market capitalisation now account for 48.7% of the ASX200, while the 20 largest companies (the ASX20) account for 63.5%. The ASX20 has been, until recently, trading on a near record multiple of one year forward earnings, as seen below. By contrast, following the selloff in mid and small capitalisation companies in recent months, the companies in the ASX200 excluding companies in the ASX20 are trading on a forward price to earnings multiple that has only been seen once in the last dozen years, very briefly during the COVID-19 panic of 2020.

ASX Index Price to Earnings (P/E) Multiples



Source: Auscap, FactSet

Historically the companies outside the ASX20 have traded on a higher multiple of earnings than the companies in the ASX20. This likely reflects the expectation that these businesses will deliver greater earnings growth over time than their larger counterparts. Over the last decade the ASX20 has delivered earnings per share growth of 0.8% per annum. The companies in the ASX200 excluding those in the ASX20 have delivered earnings growth of 4.9% per annum.

Investors logically pay a higher multiple of next year's earnings for an earnings stream that is expected to grow more quickly. The exceptions to this rule occur during periods of dislocation, like the Global Financial Crisis, COVID-19 and now the selloff of the last nine months, where smaller companies are viewed as being more susceptible to a decline in near term earnings.

There have been two primary causes for concern that have led to lower multiples in recent months. The first is developments in artificial intelligence. Artificial intelligence has the potential to upend established business models. At present all technology related businesses are seen as being at risk. The combined market capitalisation of businesses that are assumed to be at risk from these developments has fallen from over \$200bn to less than \$100bn in just the last few months.

Artificial Intelligence High Risk Index Market Capitalisation

(360, AUB, CAR, CAT, MP1, PME, TPW, TNE, REA, SDF, SDR, SEK, WTC, XRO)



Source: Auscap, FactSet

However, we think this indiscriminate selloff is creating opportunities. Not all technology-based businesses will face the same level of business model risk. The focus of our attention for each individual business is on understanding the nature of the economic moat that allows the business to generate strong returns on capital compared to peers. If this is simply a technological solution to a problem, the value of that solution may well be diminished by technological replication at low cost. A business model that uses technology to automate simple tasks or aggregate public information might be at risk if artificial intelligence allows the development of equivalent solutions at extremely low cost. The price one can charge for such a service should trend towards the cost of replication, a cost that is rapidly declining. For many larger clients of technology businesses, it may become a buy versus build analysis. This decision tree has always been there, it is just that developments in artificial intelligence may reduce the cost of technological replication and development considerably.

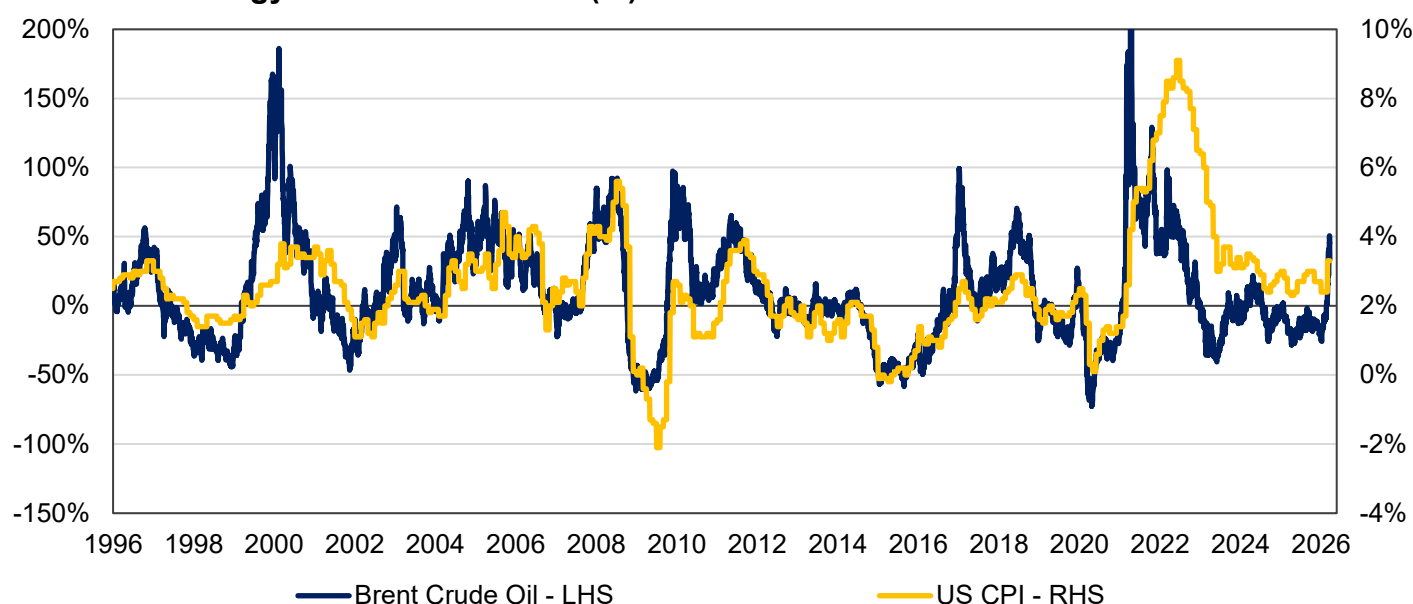
However, there are many technology related businesses where we do not think the technology is the ongoing source of competitive advantage. The technology may be a key part of the offering, but it no longer represents the sole reason the business is able to generate superior returns on capital compared to peers. We are focused on the businesses that have seen their share price fall but, based on current information, the chances of disruption appear overstated and the prospects of an acceleration in product development through the adoption of artificial intelligence may well enable the incumbent leader to improve their position relative to competitors. Technology companies we are viewing favourably include:

- Businesses that operate in highly regulated markets and/or are systems of record;
- Businesses with valuable proprietary data that cannot be scraped or replicated;
- Two-sided marketplaces with strong network effects where benefits flow from the aggregation of buyers and sellers;
- Businesses that are deeply integrated in client workflow where the risks of error outweigh the potential cost savings, particularly where the technology is adjacent to the product/service; and
- Relationship based industries where the human contact is likely to be an important ongoing feature for clients.

The uniform nature of the selloff in technology related companies is, we believe, creating opportunities for those differentiating between businesses genuinely at risk of disruption and those likely to maintain their advantage through their use of AI. We continue to allocate incremental capital towards the businesses we expect will thrive in an AI world.

The second factor affecting stocks is the conflict in the Middle East and its impact on energy prices and therefore inflation. Historically, changes in the energy price have been highly correlated with inflation, because of the direct impact of higher fuel prices and the indirect impact of higher production costs which leads to higher food and goods prices.

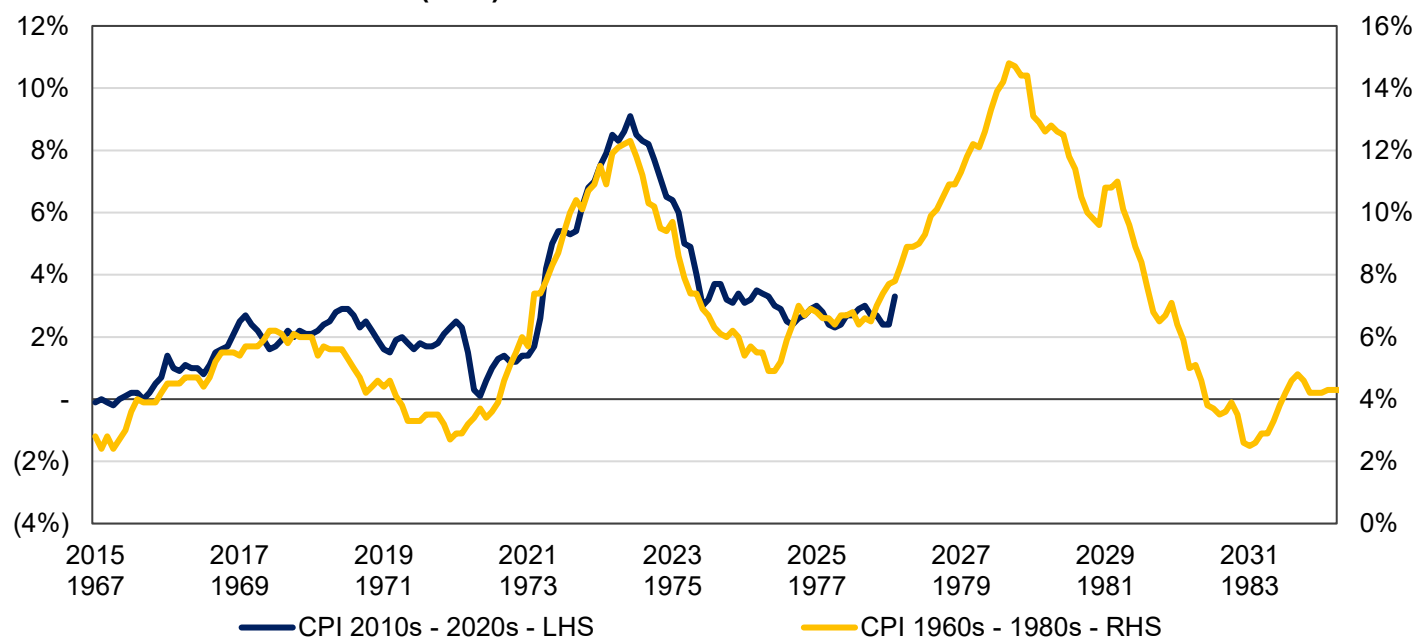
US CPI vs Energy Prices YoY Growth (%)



Source: Auscap, Bloomberg

Higher inflation has often led to central banks lifting interest rates to suppress demand and therefore get inflation back under control. The world experienced two bouts of inflation in the 1970s and early 1980s which led to materially higher interest rates. The parallels between the current environment and the two periods of elevated inflation in the 1970s-1980s are hard to ignore.

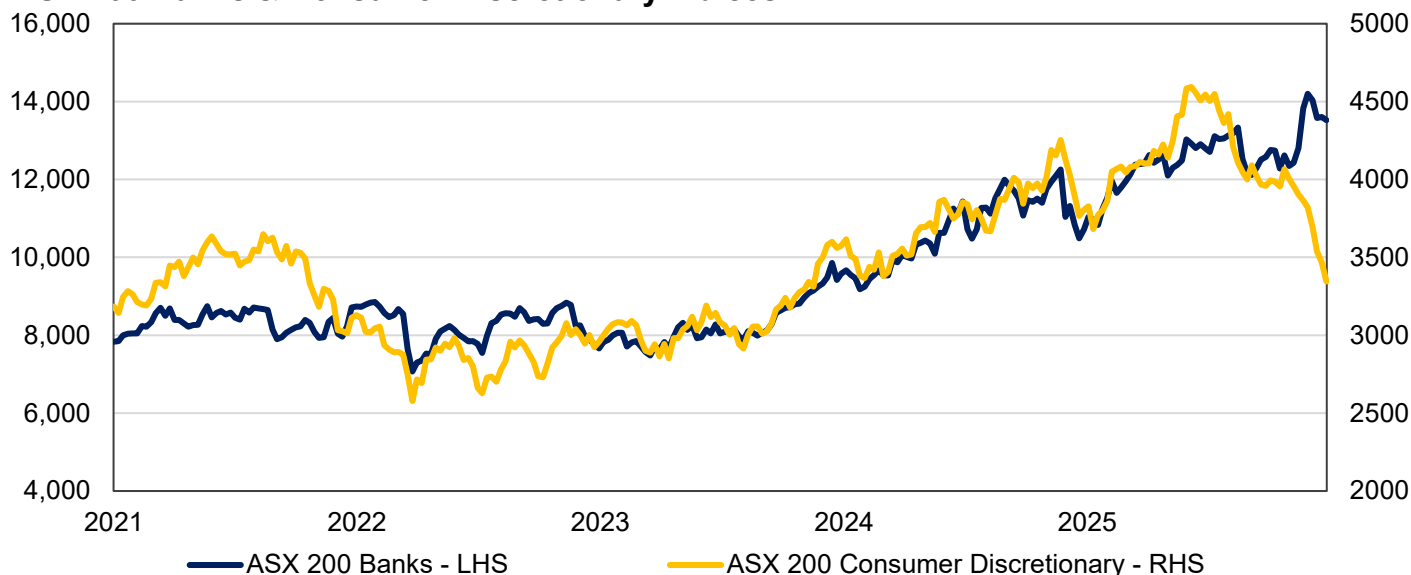
US Consumer Price Index (CPI)



Source: Auscap, Bloomberg

Market participants, fearful of the impact higher rates might have on economic activity, have sold down stocks that are perceived to be more sensitive to higher rates, such as consumer discretionary companies and real estate trusts. Albeit the disconnect between the performance of the listed retailers and the banks is unusual.

ASX 200 Banks & Consumer Discretionary Indices



Source: Auscap, Iress

There are legitimate concerns about higher inflation leading to higher interest rates. While we remain attentive to the possibility of persistent inflation above target, our investments are not premised on particular economic forecasts. The future is unknowable but high quality businesses respond quickly to changing circumstances, with their success determined more by company specific factors than the economic aggregates. Further, in relation to the current circumstances, markets are forward looking and any anticipated resolution of hostilities in the Middle East will begin to be priced into equities on the basis that an end to the conflict should gradually see an easing in pressures in the energy market. There are many companies in affected sectors that are trading on attractive multiples of earnings. We think this is a time to be looking to take advantage of opportunities in both the technology and consumer sectors. We are reminded of Warren Buffett's quote, "when it's raining gold, put out the bucket, not the thimble."

What is unique about the recent selloff is the degree to which mid and small market capitalisation companies are underperforming their larger peers. The current differential in the price to earnings ratio of the ASX20 compared to companies in the ASX200 excluding the ASX20 is extreme.

ASX 21-200 P/E Multiple Less ASX20 P/E Multiple

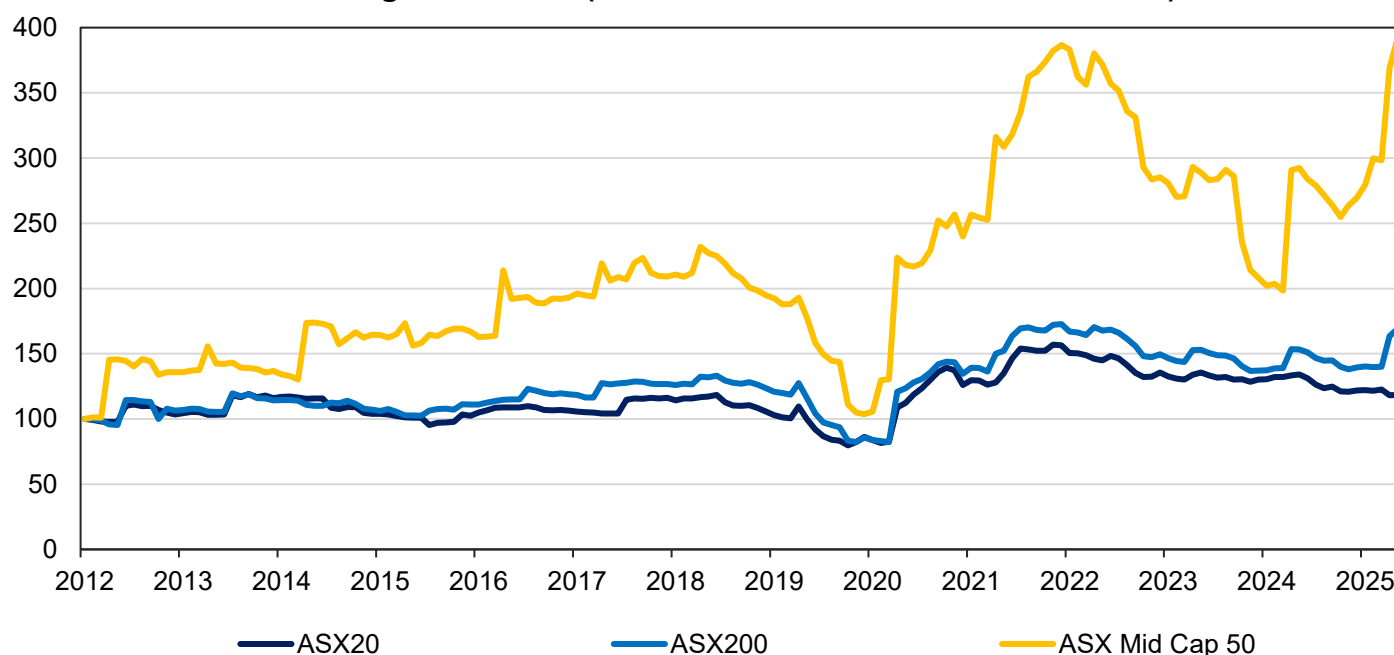


Source: Auscap, FactSet

While developments in AI and the Middle East are affecting the outlook for the economy and individual businesses, undoubtedly some of the factors contributing to this dispersion in returns are unrelated to fundamentals. The continued trend towards passive investing results in capital flowing into companies according to their current size, rather than the prospects for the business, leading to distortions as to how companies are priced. Investor and regulatory pressure for institutional managers to not underperform their benchmark leads to index replication, the simplest way to reduce this risk. This naturally leads the largest, and some of the most sophisticated, pools of capital in the Australian market to move toward passive investing. It also encourages a move to less liquid asset classes where less frequent valuations provide some protection from market related volatility, which can assist a fund to stay within established parameters. Both developments, we suspect, are not in the long-term interests of investors. It means, definitionally, that if there is a bubble in an asset class, passive funds will be compelled to participate, irrespective of how irrational it may be.

It is difficult to argue that the continued resilience of the largest companies in the market is based on a superior earnings outlook. In the most recent earnings reporting period in February, expectations for the ASX Mid Cap 50 improved considerably. This contrasts with the weak share price performance many of these businesses have experienced. By contrast, earnings expectations for the ASX20 remained subdued, and yet these companies have seen marked share price outperformance.

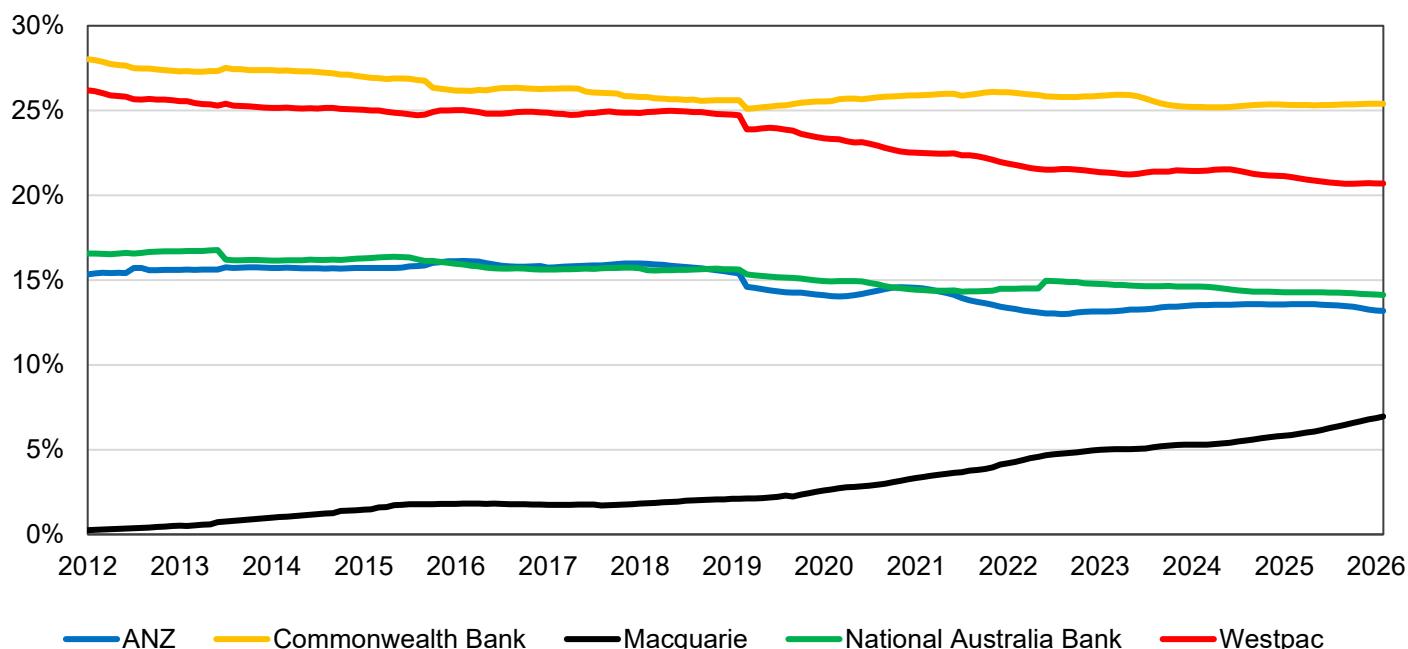
ASX200 Forecast Earnings Per Share (Rebased to 100 on 30 November 2012)



Source: Auscap, FactSet. Rebased to the inception date for the Auscap High Conviction Australian Equities Fund.

In fact, we would suggest that the outlook over the next decade for some of the largest domestic companies is increasingly challenged. The largest four domestic banks, Commonwealth Bank, Westpac, NAB and ANZ, account for 24% of the ASX200. We have written previously about the emerging unprecedented competition they face in the mortgage market from Macquarie. Here Macquarie, as the challenger, is in the unusual position of having a natural competitive advantage. With a modern technology stack based on one data platform, and a streamlined online-only business model with no legacy branch network costs, they have a lower cost, scalable business model compared to the majors. This is allowing them to offer considerably better value to both deposit holders and borrowers, compared to the major banks. On the deposit side they offer an at call rate, 4.75%, that exceeds the RBA cash rate and is unmatched by the majors in their savings and short duration term deposit accounts, let alone in their everyday banking accounts. For the borrowers in their target market, Macquarie is offering the lowest rate and compellingly fast turnaround times for the mortgage broker channel. Mortgage brokers in the December 2025 quarter were responsible for writing 76.7% of all new home loans. It is a channel that Macquarie services well and it is currently the source of more than 95% of the loans Macquarie write. Compelling offers to both deposit holders and borrowers have led to both sides of the ledger growing at 22% per annum for the past five years. As this business continues to scale, the entrenched profits of the big four banks are going to look increasingly at risk. Macquarie is a formidable competitor and the share losses look set to accelerate as Macquarie continues to scale this business.

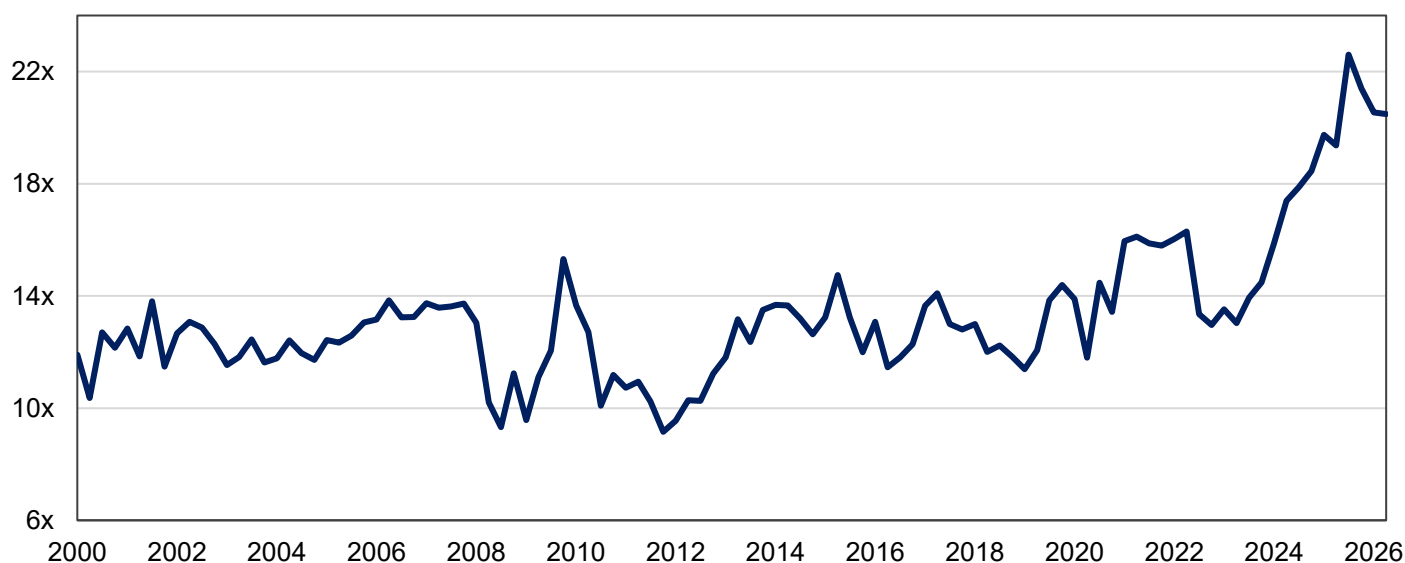
Australian Mortgage Share



Source: Auscap, APRA

It is baffling that at a time of unprecedented competition, technology disruption and economic uncertainty the big four banks are trading at near record multiples of near-term earnings. Macquarie's emergence is not a well-kept secret. Their growth is going to challenge the revenue and earnings of the major banks in the years to come. That the banks are trading at such lofty multiples at a time of imminent potential disruption speaks to the weight of capital flowing passively into the market. One in four dollars passively invested into Australian equities is buying the big four banks. We do not think this situation will continue indefinitely. We are reminded of the German proverb, "trees don't grow to the sky".

Big 4 Bank Weighted Forward P/E ratio



Source: Auscap, Bloomberg

High quality, competitively advantaged businesses with strong prospects for growing earnings at rates well above the market are currently on sale. We are focused on optimising the deployment of capital into the best opportunities. While active management has faced challenges in recent years, the current environment may well provide a fertile environment for strong active returns in the Australian market for years to come.

Auscap High Conviction Australian Equities Fund

Fund Performance*

Period	Auscap	All Ords
March 2026	(10.8%)	(7.3%)
Calendar Year To Date	(14.6%)	(2.7%)
Since Inception (Dec 2012)	428.4%	225.2%
Annualised Returns	13.3%	9.2%

Fund Exposures

March 2026 Average	% NAV	Index
Equities	97%	100%
Cash	3%	0%
Beta Adjusted Exposure ⁺	105%	100%
Positions	43	500

Portfolio Commentary*

The Fund returned negative 10.8% net of fees during March 2026. This compares with the All Ordinaries Accumulation Index return of negative 7.3%.

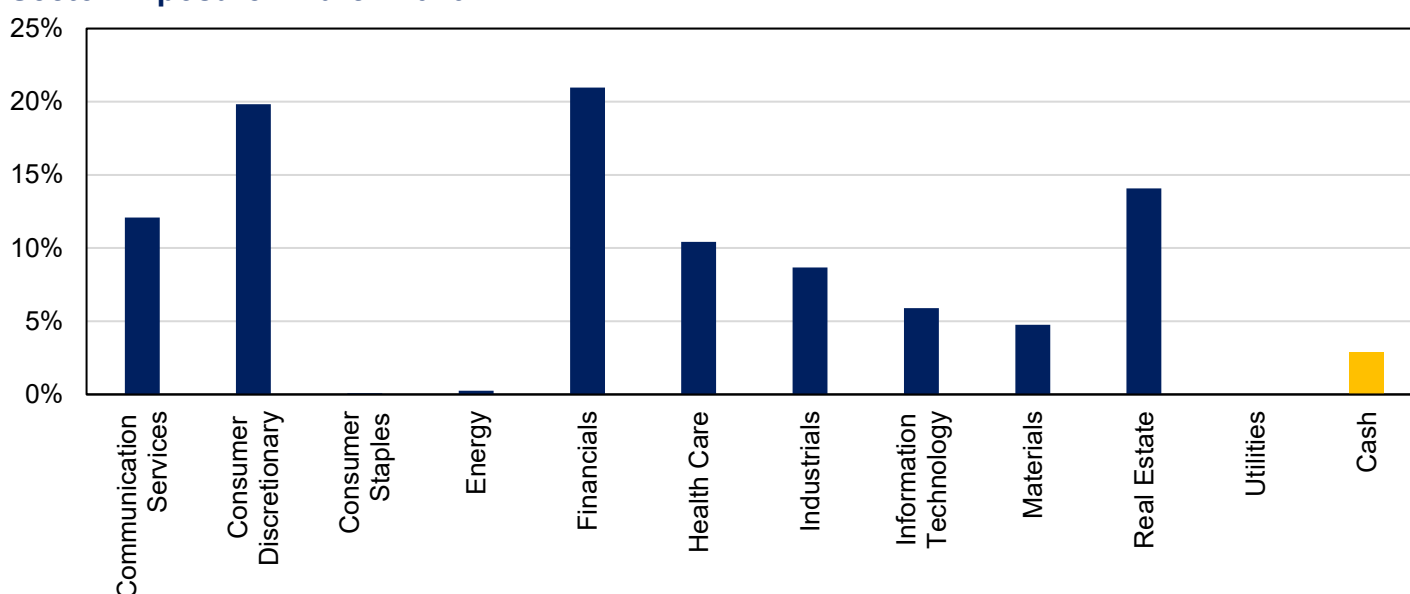
During March, the Fund's exposures to the Consumer Discretionary, Information Technology, Real Estate, Communication Services, Industrials, Healthcare, Materials and Financials sectors were the most significant detractors from returns.

Over the month, Reece, Life360, Nick Scali, CAR Group, IDP Education, Resmed, HomeCo Daily Needs REIT, Northern Star, ARB Corporation, Macquarie Group, Genesis Minerals and Sonic Healthcare were the largest detractors from performance.

Top 20 Investments[^]

ARB Corp	Magellan Financial Group
AUB Group	Netwealth Group
CAR Group	NIB Holdings
Charter Hall Group	Nick Scali
Charter Hall Retail REIT	Northern Star
HomeCo Daily Needs REIT	REA Group
IDP Education	Reece
Life360	Resmed
Lovisa Holdings	Sonic Healthcare
Macquarie Group	Steadfast Group

Sector Exposure - March 2026[#]



* Performance figures are calculated for the Monthly Class net of all fees and expenses and assuming the reinvestment of all distributions. Note, as at 1 January 2021, the Series Class was consolidated into the Monthly Class. Prior to 1 December 2024, the fund was called the Auscap Long Short Australian Equities Fund and was able to short sell and use leverage as part of its investment strategy. Past performance is not a reliable indicator of future performance.

⁺ Beta adjusted exposure adjusts the portfolio for the beta, or share price volatility, of the stocks relative to the All Ordinaries Accumulation Index.

[^] Top 20 investments in alphabetical order as at 31 March 2026.

[#] Average sector exposure during March 2026.

Auscap Ex-20 Australian Equities Fund

Fund Performance*

Period	Auscap	Index**
March 2026	(10.8%)	(10.2%)
Calendar Year To Date	(13.5%)	(10.1%)
Since Inception (Dec 2023)	24.4%	23.0%
Annualised Returns	9.8%	9.3%

Fund Exposures

March 2026 Average	% NAV	Index
Equities	98%	100%
Cash	2%	0%
Beta Adjusted Exposure ⁺	103%	99%
Positions	61	280

Portfolio Commentary*

The Fund returned negative 10.8% net of fees during March 2026. This compares with the S&P/ASX 300 Ex S&P/ASX 20 Index return of negative 10.2%.

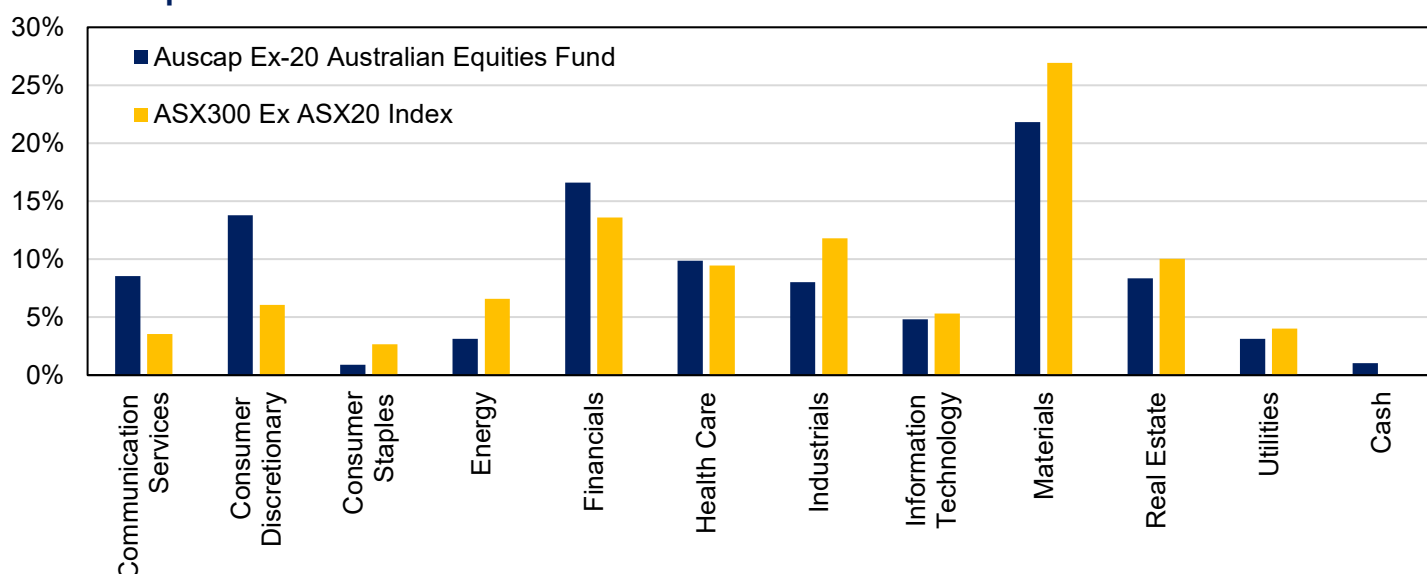
During March, the Fund's exposures to the Materials, Consumer Discretionary, Information Technology, Healthcare, Communication Services, Real Estate, Industrials and Financials sectors were the largest detractors from returns.

The Fund's holdings in Northern Star, Life360, Reece, Nick Scali, Genesis Minerals, CAR Group, Resmed, IDP Education, Vault Minerals and Ramelius Resources were the largest detractors from returns.

Top 20 Investments[^]

AUB Group	Magellan Financial Group
Capricorn Metals	Nick Scali
CAR Group	Northern Star
Charter Hall Retail REIT	Origin Energy
FireFly Metals	Ramelius Resources
Genesis Minerals	REA Group
HomeCo Daily Needs REIT	Reece
IDP Education	Resmed
Life360	Santos
Lovisa Holdings	Sonic Healthcare

Sector Exposure - March 2026[#]



* Performance figures are calculated for the General Class net of all fees and expenses and assuming the reinvestment of all distributions. *Past performance is not a reliable indicator of future performance.*

** Index used is the Benchmark for the Auscap Ex-20 Australian Equities Fund, being the S&P/ASX 300 Ex S&P/ASX 20 Index.

⁺ Beta adjusted exposure adjusts the portfolio of the Fund and of the Benchmark (being the S&P/ASX 300 Ex S&P/ASX 20 Index) for the beta, or share price volatility, of the stocks relative to the All Ordinaries Accumulation Index.

[^] Top 20 investments in alphabetical order as at 31 March 2026.

[#] Average sector exposure during March 2026.

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S&P Dow Jones Indices

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Auscap Asset Management Limited

ACN 158 929 143 AFSL 428014
Lvl 30, 9 Castlereagh St, Sydney

Email: info@auscapam.com
Web: www.auscapam.com

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