



# The case for Australian equities

## Blessed with resilience and resources

The Australian economy has proven more resilient than most in times of major economic challenges. It held up well in the face of the calamitous 1997 Asian financial crisis.<sup>1</sup> It emerged relatively unscathed from the 2008–09 global financial crisis, thanks to its robust banking system and strong demand for resources from fast-growing countries like China.<sup>2</sup> It dipped only briefly during the COVID-19 pandemic and experienced an earlier recovery than most OECD countries.<sup>3</sup>

This resilience is underpinned by the unique composition of its underlying economy,<sup>4</sup> which is also reflected in its equity market – making local shares an attractive investment opportunity. Not only does Australia have plentiful mineral and energy reserves, but its resources companies are considered leaders in technical and project delivery, and for their commitment to safety.<sup>5</sup>

The country's leading financial institutions are also highly competitive within the Asia-Pacific region, with its fund management sector particularly recognised for innovation and sophistication.<sup>6</sup>

“While we have witnessed a challenging environment in recent years, market volatility also opened new opportunities to invest in inexpensive, high-quality companies that are poised to capitalise on long-term growth trends in Australia, such as the green transition and population growth. In addition, tactical opportunities have emerged during this inflationary period among companies with strong pricing power.”

**Paul Taylor**, Portfolio Manager  
Fidelity Australian Equities Fund

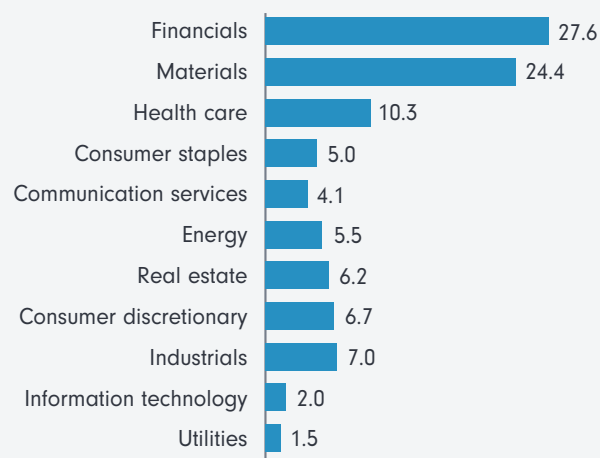
## Australia, where to from here?

With further interest rates hikes expected, the likelihood that the US and Europe will enter a recession is increasing. Still, it remains uncertain whether Australia will follow suit, with high energy costs and favourable conditions for commodities, immigration and population growth providing a cushion against recession. This should bode well for Australia's vibrant equities market – with over 2,000 listed companies, the domestic market is the world's ninth largest and has consistently been among its best performers.

The largest 200 listed companies represent over 80% of the market's total capitalisation, with the largest index constituents – such as BHP Group, Commonwealth Bank of Australia and CSL Limited – valued at over A\$100 billion.<sup>7</sup>

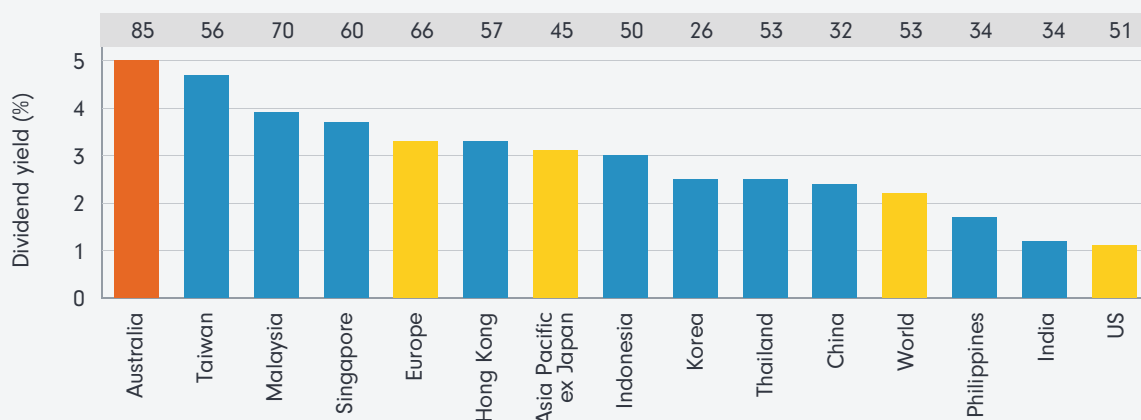
The S&P/ASX 200 sector/industry exposure in Figure 1 highlights that financial and materials make up just over 50% of the total index. Whilst the strong performance of the resources and financial services industry has contributed to the market's consistent returns, the benchmark index doesn't fully reflect the relatively stronger growth seen in sectors such as technology and health care in 2020 and 2021.

**Figure 1. S&P/ASX 200 sector/industry exposure**



Source: S&P/ASX 200 as at 30 April 2023.

**Figure 2. Average payout ratio over the last 5 years (%)**



Source: Bloomberg, Refinitiv DataStream, as at 31 December 2022.

## Don't forget the smaller end of town

And investors should remember that the Australian market is not just limited to the large end of town. In fact, the Australian small- and mid-cap segment has been home to several future leaders, which have generated value for investors as they've graduated to the large-cap arena.

One such prominent recent example is the sleep apnoea equipment technology specialist ResMed, founded in 1989, which graduated into the S&P/ASX 50 Index in September 2021, and now has a market capitalisation of more than \$47 billion.

Focused on technology and innovation, ResMed commercialised a prototype CPAP (continuous positive airway pressure) technology and scaled its production globally. Its technology helps people all over the world with sleep apnoea, COPD and other chronic respiratory diseases breathe and live better. ResMed is now a global leader in sleep technology with origins right here in Australia.

In Australia, we've witnessed other mid-cap and small-cap businesses evolve from an idea to established international businesses, including now well-known names such as Domino's and CSL.

## A greater focus on dividends

Another attractive feature of the Australian equity market is its well-established culture of dividend discipline, which includes tax effective components such as franking credits.

Over the last five years, Australian companies, on average, distributed more of their net income to shareholders than companies in the US, Europe and Asia-Pacific ex Japan (Figure 2), offering an additional source of income for investors.

## Stock story – Fidelity Australian Equities Fund



**BHP** is the largest mining company in the world and the largest Australian company by market capitalisation. The 'Big Australian', as it is colloquially known, has been a mainstay of Australian equities since it began life as Broken Hill Proprietary in 1885, merging with UK-listed Billiton in 2001.

BHP offers exposure to a diversified portfolio of commodities and long-life, high-quality assets, but its Pilbara iron ore operations currently drive the majority of earnings. Steel is critical to infrastructure and the energy transition, as is copper for the electricity grid build-out and nickel for use in EV batteries. Potash, used in fertiliser, will also be critical to feed a growing population and BHP is increasingly focused on these 'future-facing commodities', divesting petroleum and acquiring more copper through the recent OZ Minerals transaction.

Commodities are cyclical by nature, but BHP's scale, diversification, strong balance sheet and future-facing outlook has allowed it to consistently invest and grow through multiple cycles. This resilience through the cycle is why BHP is a long-term holding in the Australian Equities portfolio.

## Stock story – Fidelity Future Leaders Fund



**Altium Limited (ALU)**, an ASX-listed company, is engaged in the development and sale of computer software for the design of electronic products and an online collaboration platform to facilitate the manufacturing of them. The company is based in Australia with sales operations in the Americas, Europe, Middle East and Africa, Greater China, and Asia Pacific.

Altium software and services provide the unique bridges that connect electronic design to the electronics supply chain and the manufacturing of electronic products. With the strong early adoption of their cloud platform, they are now playing an essential and growing role in the design and making of smart products, that spans manufacturability and productivity, research and influence, and component sourcing.

Altium is a high return on capital business in a small niche market structure where there are only a few specialised global competitors. The structural growth tailwinds from the 'Internet of Things' and the deep levels of complexity in the global development of PCB (printed circuit board) design will allow Altium to grow for many years to come. In our stock selection process, the company exhibits very highly in viability, sustainability and credibility.

## Stock story – Fidelity Opportunities Fund



**Carsales.com Ltd (CAR)** is the online automotive, motorcycle and marine classifieds business in Australia. Together with its subsidiaries employing over 600 people in Australia, developing world technology and advertising solutions that drive its business. The CAR network has operations across the Asia Pacific region and has interests in leading automotive classified businesses in Brazil, South Korea, Mexico, Chile, Argentina and the United States.

Carsales is a dominant market leader with strong pricing power in Australia and multiple avenues to raise prices. The business is scaleable offshore. CAR have a strong track record in overseas expansion with additional upside in newer markets like the United States and Brazil. Although not immune from a macro slowdown, used car transactions are relatively resilient even in recessionary environments.

# Fidelity – 20 years of Australian investing expertise

Fidelity has one of Australia's largest and most experienced teams of Australian investors. With more than twenty years' experience, we offer a range of actively managed Australian share funds, offering investors the exposure that suits their investment goals.

The Fidelity Australian Equities Fund, launched in 2003 and benchmarked to the S&P/ASX 200 Accumulation Index, invests in a diversified selection of 30 to 50 companies. Designed as a long-term core holding, it aims to outperform the benchmark over the medium to long term.

The Fidelity Australian Opportunities Fund, launched in 2012, is also benchmarked to the S&P/ASX 200 Accumulation Index, and offers a more concentrated portfolio of 20 to 40 high-quality Australian companies, with an emphasis on a company's risk/return profile.

The Fidelity Future Leaders Fund invests in typically 40 to 70 mid- and small-cap Australian companies which favour attractive valuations, strong competitive positioning and sound company management.

Our Australian funds are carefully weighted for diversification across sectors and companies with the aim to manage risk in the portfolio and deliver sustained returns over time.

## Why active management is key

In uncertain markets, active investing provides the flexibility essential to navigate rapidly changing market conditions. We expect conditions to remain challenging, due primarily to inflation and geopolitical concerns.

However, market volatility may play to the advantage of active stock selectors as they can flexibly find and invest in quality and reasonably valued companies that are expected to withstand market tumult while offering growth potential. As trends shift, they may

be able to manage portfolio exposures to cushion downside risks and participate in the rebound.

With a global team of over 400 investment professionals, Fidelity is well-positioned to provide a comprehensive view of global and domestic trends across industries and markets. We apply a consistent, rigorous bottom-up process to select companies through different market cycles and create diversified portfolios designed to help Australian investors maximise the benefits of resilient homegrown opportunities.

## What are the risks?

All investments involve risk; however, Fidelity actively manages risk within its investment portfolios and employs a range of monitoring procedures with the aim of reducing overall portfolio risk. The main risks of investing in the Fidelity Australian Equities Fund and the Fidelity Australia Opportunities Fund are market risk, specific security risk and derivative risk. For the Fidelity Future Leaders fund, the main risks of investing in this Fund are increased volatility when compared to investing in larger, more established companies, market risk, specific security risk and derivative risk. For further details on the specific risks of investing in these funds, please refer to the Product Disclosure Statements.

## Like to know more?

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1. Ron Duncan and Yongzheng Yang, 'The impact of the Asian Crisis on Australia's primary exports: why it has not been so bad', Asia Pacific Press at the Australian National University, 2000-1: <https://crawford.anu.edu.au/pdf/wp00/di00-1.pdf>. 2. Credit Suisse Global Investment Returns Yearbook 2021. 3. 'International economic comparisons after a year of the pandemic', Australia Bureau of Statistics, 2 June 2021: <https://www.abs.gov.au/articles/international-economic-comparisons-after-year-pandemic>. 4. Austrade: <https://www.austrade.gov.au/benchmark-report/resilient-economy>. 5. Australian Government Department of Industry, Science, Energy and Resources: <https://www.industry.gov.au/data-and-publications/australias-national-resources-statement/the-australian-resources-sector-significance-and-opportunities>. 6. Australian Trade and Investment Commission: <https://www.austrade.gov.au/international/buy/australian-industry-capabilities/financial-services>. 7. As at September 2022, Market Index: <https://www.marketindex.com.au/asx200>.

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