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Australian Small Companies – FY24 Earnings Season Observations

With another reporting season behind us, our specialist Australian Small Companies partner, Flinders Investment Partners, shares some observations from the FY24 results season. And despite ongoing cost of living pressures and a 'higher for longer' interest rate environment, more companies overall delivered positive surprises.

This information has been prepared by Flinders Investment Partners, investment manager of the Flinders Emerging Companies Fund.

FY24 Reporting Season Overview

With another reporting season behind us, below are some observations from the FY24 results season. A key reflection is that despite so many negative headlines in recent months, the negativity simply did not translate to what listed companies reported. For the broader market, 'beats' outnumbered 'misses' slightly by a ratio of 10:9. So despite 'ongoing cost of living pressures' and a 'higher for longer' interest rate environment, more companies overall delivered positive surprises.

The Australian consumer continues to be resilient, as does the overall Australian economy. Banks reported benign trading updates, which have been taken positively (all major banks share prices are currently trading at all time or multi-year highs!). Banks aren't raising loan loss provisions yet, as the arrears cycle is tracking to banks' expectations.

Optimistically Cautious

Having said all of the above, the outlook is still understandably cautious. Generally speaking, companies are citing a tough macro picture and ongoing cost challenges, but perhaps this is acknowledgement of the uncertainty.

It's true that expectations for Australian GDP have been falling for a while (2024 GDP growth estimates were down 11bp in the last three months to +1.27%, and 2025 GDP growth estimates down 6bp to +2.17%), but these are backward looking; reporting season demonstrated that there are tentative signs that activity levels have already bottomed. The stimulatory Federal Budget and tax cuts should provide some support, and rate cuts over the next 12 months should help sentiment and provide a tailwind for share market gains.

The Worst is Behind Us?

The retail sector was where a lot of the resilience was demonstrated, especially given that many of the listed retailers are at the pointy end of consumer behaviour. Commentary was consistent across the retailers within the sector indicating that the trough in consumer activity might be behind us, given that sales in the first few weeks of FY25 showed growth of around 4% compared with the same period last year. Keep in mind that recent tax cuts effective from 1 July has boosted household incomes.

The growth sectors of Technology and Healthcare had the most positive EPS surprises and were clear winners. Domestic cyclicals (including industrial service companies) were the next group showing positive EPS surprise. Energy was the worst sector.

Interest and depreciation & amortisation charges surprised to the upside (vs consensus estimates) for capex heavy and geared companies. So, while EBITDA might have been in-line, NPAT/EPS downward revisions were common. However, interest rate headwinds should pass as rate cuts come to fruition.

Small v. Large Cap Earnings Outlook

Focusing on Australian Small Companies, a few observations below based on Factset consensus estimates. Overall, the Small Ordinaries Index saw EPS upgrades to FY24 and FY25:

- FY24 EPS growth was upgraded by 1.9% to -6.5%
- FY25 EPS growth was upgraded by 4.2% to 28.4%

Interestingly, while there were more companies across the market that 'beat' expectations than 'missed', in aggregate for Large caps (ASX100 index), EPS forecasts were downgraded:

- FY24 EPS growth was downgraded by -2.2% to -3.4%
- FY25 EPS growth was downgraded by -1.2% to 2.1%

As summarised in the table below, Small companies look compelling, with EPS growth at 28.4% for FY25 at 17x PE; growth is superior to Large caps (2.1% EPS growth) and Mid-caps (11.6% EPS growth), while at a discount to Large caps (18.3x PE) and Mid-caps (20.2x PE).

2025	ASX 100	Mid Cap	Small Ords	XSI	XSR	portfolio
EPS GROWTH	2.1%	11.6%	28.4%	15.4%	78.4%	26.5%
PE	18.3	20.2	17.0	19.4	12.4	13.9
DIVIDEND YIELD	3.4%	2.3%	3.1%	3.3%	2.3%	2.7%

It's important to note that pockets of opportunity continue to exist in today's landscape to find high-quality small companies. The Fund is well positioned with similar strong growth characteristics to the Index, while at a material discount of 13.9x P/E versus the Index of 17xP/E. This gives us confidence that our portfolio is well positioned looking ahead.