

Investing with discipline: a closer look at risk, valuation and long-term returns

Central to our goal of delivering competitive, risk-adjusted returns is how we understand and manage risk. Our focus is on navigating deeper, long-term structural challenges and opportunities with resilience.

Australia is a particularly concentrated market, and financial services and materials dominate almost half the index. We selectively invest in companies within these sectors that meet our standards for quality and ethical responsibility. Of the 42 financial companies and 60 materials companies represented in the index, we own eight financials and four miners. Our strategy implements a limit on individual stocks of +/- 5% relative to the index to ensure both caution and opportunity are reflected in our positioning.

Our relative position in Commonwealth Bank of Australia CBA provides an example of our measured approach. We currently hold about 8% of the portfolio in this company, which constitutes 12% of the index. Despite the stocks continued price rise, our analysis indicates the market is overvaluing the company.

Why we’re not chasing the rally

CBA trades at a valuation premium that exceeds what fundamentals alone would justify.

- Price-to-earnings: nearly double that of its domestic peers
- Dividend yield: among the sector’s lowest
- Price-to-book: twice as expensive as the next highest bank and three times the global sector average.

Some of this premium is warranted – CBA is a well-managed, tech forward bank with a leading share of customers and deposits and is run by a strong management team. However, this premium has continued to expand, and when valuation metrics stretch so far beyond reasonable historical ranges, experience shows us that mean reversion tends to follow.

Non-fundamental flows

Short-term factors, such as political uncertainty in the United States has prompted capital to shift into other developed markets, disproportionately benefitting Australian financials due to their significant weight in global indices like the EAFE. With passive investment strategies on the rise - US passive funds received \$900bn in inflows during 2024, while \$165bn flowed out of active funds¹ – CBA has benefitted from this trend.

Remaining patient and disciplined

Political environments change quickly, and global capital can shift just as rapidly. While we can’t predict the timing, we maintain confidence that fundamentals will eventually reassert themselves. Our long-term view means that we have patience to look beyond transitional fluctuations and focus on companies exposed to enduring trends.

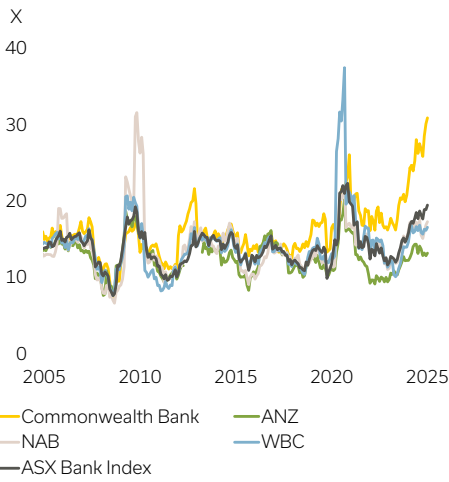
QBE and Suncorp are benefitting from rising insurance premiums, and QBE is also making progress towards growing its profitability in North America. Macquarie Group offers diversified exposure to global themes such as digital infrastructure and the energy transition.

Conclusion

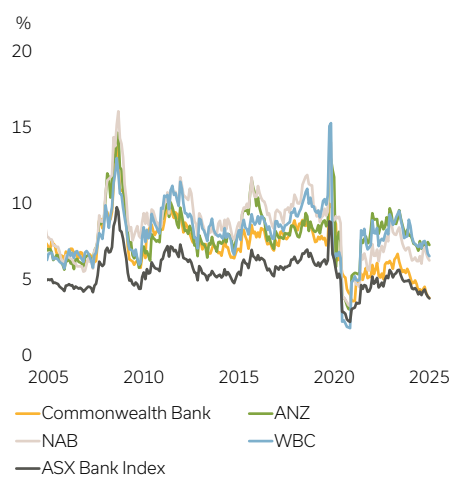
Our underweight position in CBA reflects a considered conviction. We have strong faith that current valuation levels are unsustainable, but remain measured in our exposure, given the short-term unpredictability of market flows.

Our investment process - rooted in rigorous analysis, collaborative decision-making, and long-term thinking – is built to achieve consistent, ethical, and competitive performance. We remain confident that our disciplined approach can resist short-term pressures and deliver long-term returns.

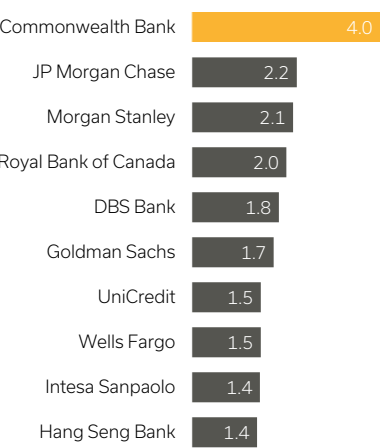
Price to earnings



Gross dividend yield



Price to book value



¹Morningstar Direct Asset Flows. Chart data source: Bloomberg. Data to June 2025.

This information is provided by Uniting Ethical Investors Limited (ABN 46 102 469 821) (AFSL 294147), trading as U Ethical. U Ethical can be contacted on 1800 996 888 or by mail and in person at Level 6, 130 Lonsdale Street, Melbourne VIC 3000.

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