Investment Newsletter – May 2026

Australian Federal 2026/27 Budget…

Welcome to the May 2026 letter.

2026/27 Federal Budget. The Australian government handed down its most recent Federal Budget, which has caused some angst among investors and the wider population. This is evident from the recent Newspoll data, with just 11% of respondents saying they expect to be better off from the recent Budget statements. According to the data, this was the weakest post-budget result since 2014, with 52% of the respondents stating they would be worse off.

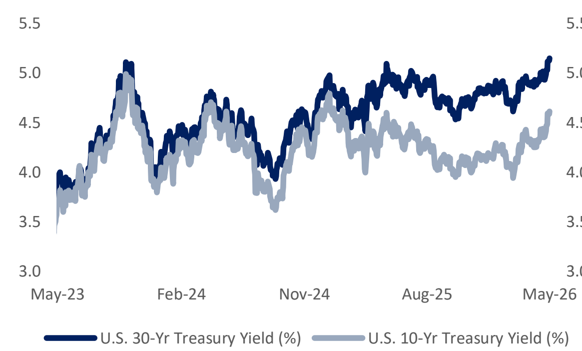
Most controversial – changes to Negative Gearing and Capital Gains Tax. The Labor government is proposing changes to the capital gains tax (CGT) including the removal of the 50% CGT discount (to be replaced by cost base indexation) and a minimum 30% tax on capital gains (targeting Discretionary Trusts which assist in splitting income among family members). There is also reform to Negative Gearing. For properties bought after 12 May 2026, deductions for investment losses will only be allowed for new builds. Properties which are already negatively geared will be exempt. These reforms were pitched to address intergenerational inequality and help younger Australians to get into the property market. However, the pushback is that these tax reforms disproportionately disadvantage younger Australians looking to build wealth through assets such as shares and start-up businesses. Additionally, given the reform to negative gearing is grandfathered, it will benefit the baby boomers/existing investors who will retain the tax benefit.

Potential impact for markets and sectors. It is difficult to say with confidence what the first order and, more importantly, second order impacts from the budget announcements will be. However, below we provide some thoughts:

- Consumer confidence is likely to be impacted, which could lead to a pullback in consumer spending – a negative for consumer discretionary stocks.
- The change to negative gearing is expected to moderate house price growth initially, which is likely to land a hit to consumer confidence and the wealth effect.
- In our view, there wasn't much in the budget which could provide the Reserve Bank of Australia (RBA) any room to consider potential interest rate cuts (if anything, the bias remains to the upside), even though Australia's budget deficit remains favourably positioned relative to developed world averages. With the budget slightly tilted towards expansionary, we would think bond yields (and therefore borrowing costs) are likely to remain elevated.
- As noted above, the negative gearing changes are likely to slow down the property market. This will impact the banks (with credit growth slowing, competition will increase among the major banks, leading to potentially greater margin impact), property plays such as REA Group and PEXA Group. It will also likely cause headwinds for developers like Stockland and Mirvac.
- More broadly, should property as an investment become less favourable due to the removal of tax concessions, investors may seek out listed companies as an alternative investment. More specifically, investors may favour dividend paying companies over high growth companies (which may require more turnover and therefore higher tax).

U.S. sovereign yields jump higher. The U.S. long-term Treasury yields – which are a key input to asset prices and valuations across the globe – experienced a material spike last week. The 30-year Treasury yield jumped well above the 5.0% level. Oil is back above the US$100 level, as a potential resolution between Iran and the U.S. remains very much elusive. It is very interesting that we are more than halfway through May and the Strait of Hormuz – a key corridor for global energy supply – remains closed. The recent spike in U.S. long-term bond yields above key sentiment levels (10-yr yield greater than 4.5% & 30-yr yield greater than 5.0%) may finally indicate that investors are starting to worry. The summit between U.S. President Donald Trump and Chinese President Xi Jinping failed to yield any material, tangible outcomes on the Iran issue.

Figure 1: U.S. long-term yields



Source: Bloomberg, Banyantree

U.S. reporting season was a standout. We feel like we do need to balance the doom & gloom discussed above (even though it wasn't pitched that way!) with some positive news. Despite the challenges facing the global economy, U.S. companies – many of which derive revenue and earnings from around the world – reported a standout quarterly reporting season. Investors often accuse sell-side analyst research as being overly bullish in their future earnings estimates. However, the latest quarterly earnings results have completely blown away consensus earnings expectations. In fact, at the time of writing, for the latest quarterly earnings in the U.S., ~82% of the companies have reported earnings which came in ahead of market expectations and in aggregate have beaten these expectations by ~18%. In growth terms, the earnings growth rate for the first quarter is running at ~25%, more than double the 12% earnings growth analysts were looking for at the start of the period. Sure, a large part of this growth is driven by the technology sector, with the Magnificent 7 forecast to deliver significant earnings growth. But the rest of the market is also delivering decent growth. Of the 11 sectors, all bar one (healthcare) are delivering positive earnings growth for the first quarter. Any wonder why markets continue to hold up?

GLOBAL MARKETS OVERVIEW

	Units	Month End Value	Price Performance (% Chg) 1-day	1-mth	6-mths	1-year
Developed Markets Equities						
ASX 200	AUD	8,666	-0.24%	2.17%	-2.43%	6.64%
ASX 200 Futures	AUD	8,668	-0.32%	1.82%	-2.98%	5.89%
Dow Jones	USD	49,652	1.62%	7.14%	4.39%	22.09%
S&P 500	USD	7,209	1.02%	10.42%	5.39%	29.45%
Stoxx Europe 600	EUR	611	1.38%	4.83%	6.89%	15.89%
FTSE 100 (UK)	GBP	10,379	1.62%	1.99%	6.81%	22.18%
DAX (Germany)	EUR	24,292	1.41%	7.11%	1.39%	7.98%
CAC (France)	EUR	8,115	0.53%	3.81%	-0.08%	6.86%
Nikkei 225	JPY	59,285	-1.06%	16.10%	13.11%	64.47%
Emerging Markets Equities						
MSCI Emerging Markets	USD	1,600	-1.13%	14.53%	14.17%	43.80%
Shanghai Composite	CNY	4,112	0.11%	5.66%	3.98%	25.41%
South Korea	KRW	6,599	-1.38%	30.61%	60.65%	158.11%
Taiwan	TWD	38,927	-0.96%	22.71%	37.87%	92.37%
Brazil	BRL	187,318	1.39%	-0.08%	25.26%	38.69%
South Africa	ZAR	107,229	1.16%	0.88%	5.19%	27.31%
Foreign Exchange						
AUDUSD	Currency	0.7201	1.19%	4.36%	10.02%	12.48%
AUDGBP	Currency	0.5294	0.23%	1.46%	6.40%	10.22%
AUDEUR	Currency	0.6138	0.72%	2.78%	8.18%	8.60%
AUDCNY	Currency	4.92	1.01%	3.46%	5.52%	5.55%
Commodities						
LME ALUMINUM 3MO ($)	USD/mt	3,474	-0.42%	0.20%	20.46%	44.78%
LME COPPER 3MO ($)	USD/mt	12,987	-0.13%	5.28%	19.28%	42.32%
LME NICKEL 3MO ($)	USD/mt	19,468	1.02%	13.78%	27.86%	26.27%
SILVER FUTURE Jul26	USD/oz	74.03	2.69%	-1.92%	49.56%	115.19%
ICE Newc Coal Fut Jul26	USD/mt	139.05	-0.32%	-6.65%	18.95%	14.54%
62% Import Fine Ore in USD	USD/t	101.40	0.00%	-0.70%	-0.06%	8.08%
Gold Spot $/Oz	USD/oz	4,618	1.54%	-1.08%	15.36%	40.42%
WTI Oil	USD/bbl	105.07	-1.69%	12.78%	75.00%	83.43%
Henry Hub	USD/mmBtu	2.64	1.15%	-15.92%	-26.05%	-15.38%
Corn	USD/Bu	464.75	-0.38%	1.53%	7.71%	-0.54%
Wheat	USD/Bu	623.75	-2.88%	1.22%	16.81%	21.59%
Fixed Interest						
10-Yr Bond Yield						
Australia	AUD	5.06%	+0.07%	+0.09%	+0.77%	+0.90%
US	USD	4.37%	-0.06%	+0.05%	+0.29%	+0.21%
Germany	EUR	3.04%	-0.07%	+0.03%	+0.40%	+0.59%
Japan	JPY	2.53%	+0.05%	+0.17%	+0.86%	+1.21%
Italy	EUR	3.86%	-0.10%	-0.05%	+0.48%	+0.30%
Australian Rates						
Cash Rate	AUD	4.10%	+0.00%	+0.25%	+0.50%	-0.25%
90-Day BBSW	AUD	4.38%	+0.02%	+0.08%	+0.74%	+0.50%
180-Day BBSW	AUD	4.78%	+0.06%	+0.01%	+0.91%	+0.88%
CBOE Options						
CBOE VIX (Volatility Index)	Index	16.89	-10.21%	-33.11%	-3.15%	-31.62%

Data as of 30 April 2026

ECONOMIC NEWS

• **Australia**. Consumer confidence tumbled in April, registering the biggest monthly decline since the onset of the Covid-19 pandemic, with near-term expectations dropping back to 2022–23 lows, as soaring fuel prices coupled with another interest-rate increase brace consumers for a return to the extended period of weakness seen during the 2022–24 inflation fight. Private sector activity stabilized in April after March's decline with composite PMI moving above the neutral threshold, as a modest recovery in services was offset by continued weakness in manufacturing amid soft domestic demand, rising cost pressures, and supply chain disruptions linked to Middle East tensions. Inflation remained above the top of the RBA's 2-3% target band in 1Q26 with trimmed mean CPI rising +3.5% y/y, as higher fuel costs from Middle East supply disruptions compounded already-elevated price pressures. Home prices rose at the slowest pace since January 2025 in April, due to large declines in Sydney and Melbourne, which fell -0.6% apiece as rising borrowing costs hurt demand, while Perth was the outperformer, clocking +2.1% growth followed by Brisbane and Adelaide recording rises of more than +1%.

• **U.S.** The FOMC voted 8-4 to leave its benchmark interest rate unchanged in a target range of 3.5-3.75% but revealed a deepening division over the outlook for policy amid increased uncertainty caused by the conflict in the Middle East, marking the first time since October 1992 that four officials dissented against a FOMC decision with "vast majority" of officials expressing it may take longer to return inflation to the Fed's 2% goal, and that upside risks to inflation and downside risks to employment were elevated. The economy expanded at a slower pace than previously estimated in 4Q25, with inflation-adjusted GDP increasing at a +0.5% annualized rate.

• **China.** The economic growth rebounded more than expected in 1Q26, with GDP expanding +5% y/y, the fastest in three quarters, as rapid growth in tech sectors continued to drive industrial production as well as exports, which surged +15% y/y, and fixed-asset investment gained +1.7% y/y, while household spending per capita only grew +2.6% in price-adjusted terms, its worst pace of year-to-date expansion since 4Q22 as wage incomes increased the slowest since late 2022. Industrial firms saw faster growth in earnings in 1Q26, with profits rising +15.5% y/y, marking the biggest pickup for the period in 5-years. Factory activity worsened less than forecast in April, with manufacturing PMI remaining in expansion powered by demand from overseas while non-manufacturing PMI slipping to contraction, as construction activity suffered its biggest slump since the early stages of the Covid-19 pandemic with the subindex of construction falling to the lowest level on record excluding February 2020, while services sector fell back into contraction.

• **Europe.** The ECB left the deposit rate unchanged at 2% as officials haven't seen convincing evidence in the data of the need to tighten monetary policy with the ramp-up in oil and natural gas costs "certainly" not yet triggering so-called second round effects, with President Christine Lagarde signalling the bank will consider a possible interest-rate hike in June while noting stagflation is a label that belongs to the 1970s and shouldn't be used to describe the current predicament of the euro zone as the current juncture as a "completely different situation" from the 1970s, citing differences in inflation, unemployment, and monetary and fiscal frameworks. The euro-area economy slowed at the start of 2026, with 1Q26 GDP rising +0.1% q/q (0.8% y/y).

• **Japan.** The BOJ left its benchmark interest rate unchanged at 0.75% in a 6-3 split vote, representing the biggest divide under Ueda's governorship and increasing the likelihood of a hike in June, with Governor Kazuo Ueda casting doubt on the economy's outlook, saying there's now less likelihood the BOJ will meet its outlook for the economy and prices, as the bank raised its forecast for 2026 core inflation by +90bps to 2.8% and for 2027 by +30bps to 2.3% while lowering 2026 and 2027 GDP growth outlook by -50bps and -10bps to +0.5% and +0.7%, respectively. Consumer sentiment weakened further in April to the lowest level in 1-year. Private sector growth slid to its weakest pace in 4-months in April with business confidence regarding future output weakening for the second consecutive month, falling to its lowest level since August 2020.

THE LONG READ

APRA's Hybrid Wind-Up…

On the morning of Tuesday, 10 September 2024, the Australian Prudential Regulation Authority released a discussion paper and a short media statement. The Chair, John Lonsdale, set out a proposal to phase out Additional Tier 1 capital instruments. These are the bank securities most Australian retirees know as hybrids. APRA confirmed the decision three months later and finalised the framework changes on 4 December 2025. The new prudential standards take effect on 1 January 2027. By 1 January 2032, the bank hybrid market will no longer be a feature of Australia's banking system. If you hold bank hybrid securities, your next call notice will be a decision you have not had to make for 15 years. Roughly $41 billion of these securities sit in Australian portfolios. Much of that is owned by retirees who bought them for the income. The hybrids you already own will continue to pay coupons and be called on schedule. But when the cash comes back, the same instrument will not be there to roll into. Over the next six years the existing $41 billion stock will leave the market on the same schedule it always would have, just without anything coming in behind it.

Why APRA changed its mind. For 15 years, Australian retail investors held an instrument that paid like a bond, was sold like a bond, and traded with most of the day-to-day price stability of a bond. The reason it paid more than a bond was that, in the moments that mattered, it was not a bond. It was a piece of the bank's loss-absorbing capital. The yield on the hybrid was never extra. It was the price of an option the holder had implicitly sold to the regulator. APRA's view changed because overseas, in March 2023, that option got exercised.

The Swiss authorities forced UBS to absorb the failing Credit Suisse. As part of the rescue, 16.5 billion Swiss francs of Credit Suisse AT1 hybrids (Additional Tier 1, the international name for hybrids of the kind APRA regulates) were written down to zero. Equity shareholders, who in the standard order of recovery should take losses before hybrid holders, received some value in the deal. Hybrid holders received nothing. The order of recovery that the prospectuses had described in clear English turned out, when stress arrived, to be more flexible than the marketing material had suggested. The case is not over. In a partial ruling on the lead case in October 2025, the Swiss Federal Administrative Court found that FINMA's write-off decree lacked a proper legal basis. FINMA has appealed to the Federal Supreme Court. The bonds remain written down while the case runs, and thousands of bondholders are still waiting for resolution. The point for Australian investors is not the final court outcome. It is that the instrument has created exactly the kind of legal uncertainty APRA says it wants to avoid.

APRA looked at what happened in Switzerland and drew a structural conclusion. The hybrid had not done what hybrids were supposed to do in a crisis. It had introduced legal complexity, contagion risk, and an outcome the system was politically unwilling to repeat. Phasing the instrument out is not a verdict that hybrids have failed Australian investors. They have not. The decision is the regulator declining to find out, in the next crisis, whether the instrument can be made to work in time.

What the yield was actually paying for. The honest version of the 15-year track record is this. Hybrids paid a real yield premium over term deposits.
Capital was returned on the expected schedule. The major banks did not approach non-viability, and APRA did not pull the kill switch – that is, if APRA determines that a bank has reached a point of non-viability, the bank's hybrid converts into ordinary shares at a set price or if conversion is not workable, the hybrid is written off entirely. For investors who needed franked income and read the prospectus carefully, the trade compensated for the risk it asked them to carry. A piece on hybrids that does not concede those points is not credible. The honest version is narrower. The trade worked while two conditions held: the bank stayed well away from non-viability, and the regulator stayed willing to leave the kill switch unused. Both conditions held in Australia for 15 years. The Swiss episode is APRA's evidence that the second condition cannot be assumed for the next 15. APRA is making the call now, while the market is calm, rather than under stress.

Where the income goes from here. Hybrids bundled two things: a bond-like income stream, and an equity-like loss-absorption mechanism. The premium yield was the price of the bundle. The work now is to decide, for each portion of your income, whether bond risk or equity risk should be carrying it, and to hold the instrument that matches the choice. There is no single right answer. There is a right answer for your circumstances, and it usually comes down to which of three priorities matters most.

If your priority is preserving capital. Term deposits, cash and absolute return fixed income strategies which target very low volatility. However, these securities offer materially lower yield compared to major-bank hybrids. But you gain capital certainty. The trade-off is inflation. Over time, capital that does not grow loses purchasing power. For a retiree drawing income, that is a real cost, not a theoretical one.

If your priority is keeping the franked income. Major bank ordinary shares can pay franked dividends, but current cash yields vary materially. CBA is low 3%, while ANZ, NAB and Westpac are around the mid 4% before franking. Franking levels also vary: CBA, NAB and Westpac's latest interim dividends are fully franked; ANZ's 2026 interim dividend is 75% franked. For a fully franked dividend, the grossed-up yield is about 43% higher than the cash yield. You take on equity volatility (share prices move, sometimes sharply) and the dividend is not contractual. The board can cut it.

If your priority is keeping bond-like income. Tier 2 subordinated bonds, or a listed fund holding them sit higher in the bank capital queue than hybrids and behave more like a bond day-to-day. Senior bank bonds usually pay less than Tier 2 but rank higher if the bank gets into trouble. What you give up is some yield against the hybrid. What you reduce is the equity-loss tail that hybrids quietly carried.

For most retirees, the realistic choice is not three-way. It is usually a combination of two.

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