In the Markets Now

Earnings explosion

We believe in the old saying: a picture is worth a thousand words. Here, we aim to recap recent market action and provide some perspective to investors.

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WHAT DRIVES LONG-TERM STOCK OUTPERFORMANCE?

Quick question: What is stock? I ask this not as some sort of trick or brain twister, but instead as part of an effort to better get at the core of what investing is. And with some parts of the market looking like a casino, I hope it's a worthwhile effort.

At its most basic, stock is just an ownership share in a company. Ok, but it's not like a share of Apple stock comes with keys to their Cupertino headquarters and a corner office (…I don't think), so what does that actually mean? Pretty simply, owning stock (aka equity) entitles one to a portion of a company's earnings in perpetuity. And while that might seem ambiguous (especially for non-dividend-paying firms), the takeaway is that there is a tether between a stock's price and its earnings. Perhaps not in the short- or even the medium-term (stock prices can be far more volatile than their underlying fundamentals), but in the long-term, the market is a weighing machine—the fundamentals must matter.

Ok Ross, thanks for the Finance 101, but get to the point. Right. Well, with investor focus spread across everything from geopolitics to the Federal Reserve's tapering language, it sometimes pays to step back and just see how US company earnings are doing. And the answer is…outstanding. Just to run through a few numbers from the quarter ended March 31:

- **86% of companies have reported earnings per share (EPS) above estimates.** This would mark the highest percentage since FactSet began tracking the metric in 2008.
- **In aggregate, earnings are coming in 23% above estimates.** This is well above the 5-year average of 7% and would mark the second-highest percentage since FactSet began tracking this metric in 2008 (spotting a trend?)
- **The blended earnings growth rate for Q1 is 50%.** This is versus an estimated growth rate of 24% just six weeks ago (and would mark the highest year-over-year earnings growth since 2010).
- **The S&P blended profit margin for 1Q21 is 13%.** This is above the 5-year average of 11% and would mark the highest net profit margin reported by the index since FactSet began tracking the metric in 2008.
- **Analysts project double-digit earnings growth for the remaining three quarters of 2021**. Earnings growth is expected to peak in Q2 2021 at 59%. See our chart to the right (via FactSet) and Strategas' take here.

- **Companies are issuing strong outlooks.** At this point in time, the percentage of firms giving positive earnings guidance (an in-house forecast given ahead of actual results) is 59%, which is well above the 5-year avg. of 35%.

Not half bad at all. Now, stocks are forward-looking animals, so a lot of this strength is already priced into a market near all-time highs. But it's still comforting to know that one of the key underpinnings of the entire market—corporate earnings—are justifying the price to an extent. Hard for me to see a bubble in stocks when companies are performing so strongly.

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