USEFUL notes – It's beginning in the US the earnings reporting from Q1: the expected variance is +24% when compared to last year's low levels. Estimates on trimestral growth remains modest, leaving space for positive surprises.

This week in the US (and Europe towards the end of April) will begin the business earnings reporting season for the 1st quarter. After many positive surprises from the last three seasons, the progress of vaccination campaigns and fiscal policy stimuluses, analysts have increased their expectations on earnings growth (to a yearly 24%) and profits (to 6%) not only for the 1st quarter, but for all of 2021.
The future numbers up for publication in the next days will tell us if analysts kept on maintaining an overly cautious profile, despite the increasing expectations. This is still probable, considering the economic recovery has always been seen as increasing after data-led improvements, especially the ones from the end of the quarter.

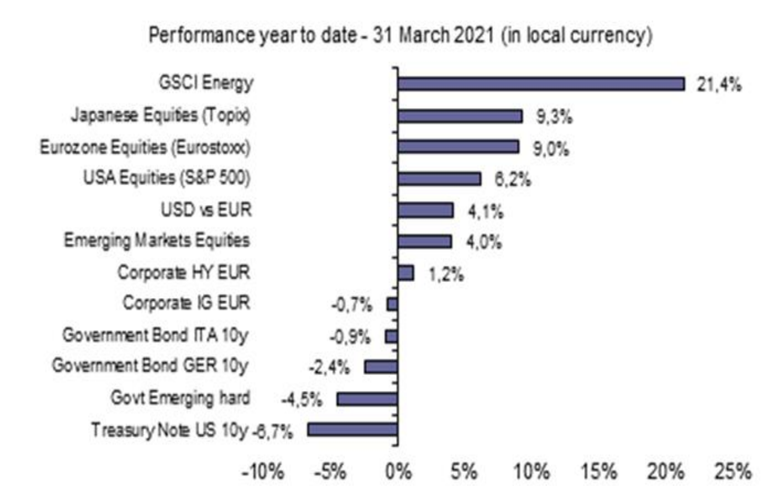
Market's performance in 2021's 1st quarter

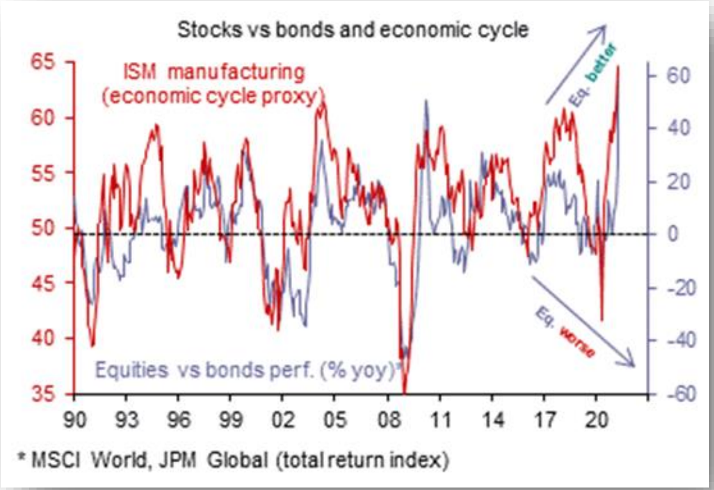
Expectations for normalization in the economic recovery and for a raise in inflation were the themes that guided the market for the whole of the 1st quarter. Said expectations are more evident in the US, considering the progress in the vaccination campaign (allowing business reopening) and the continued support for the economy from fiscal policy.

The quarter observed US rates rising strong (with the ten-year rate to 1.7%, at pre-pandemic level) and hence, negative performances on financial activities closely linked with US rates (corporate bonds IG US and governmental bonds in emerging markets).

Rising rates did not stop stocks from going up: the normalization effect has been way more than compensated by the expectation of a strong recovery for business earnings. US' stock market reached new all-times high in the last quarter, while Europe interrupted its under-performance phase from last year, benefitting from a sectorial division, more exposed to cyclic themes, in addition to expected accelerations of vaccination campaigns. Emerging stock markets lag behind, being more sensible to rising rates.


Equity markets: USA, Eurozone, Emerging
(local curreny indexes)
S&P500
Emerging
Eurostoxx
205
195
185
175
165
155
145
135
125
115
105
95
85
75
16
17
18
19
20
21


Performance year to date - 31 March 2021 (in local currency)
GSCI Energy 21,4%
Japanese Equities (Topix) 9,3%
Eurozone Equities (Eurostoxx) 9,0%
USA Equities (S&P 500) 6,2%
USD vs EUR 4,1%
Emerging Markets Equities 4,0%
Corporate HY EUR 1,2%
Corporate IG EUR -0,7%
Government Bond ITA 10y -0,9%
Government Bond GER 10y -2,4%
Govt Emerging hard -4,5%
Treasury Note US 10y -6,7%
-10%
-5%
0%
5%
10%
15%
20%
25%


Stocks vs bonds and economic cycle
ISM manufacturing
(economic cycle proxy)
Equities vs bonds perf. (% yoy)*
Eq. better
Eq. worse
65
60
55
50
45
40
35
60
40
20
0
-20
-40
-60
90
93
96
99
02
05
08
11
14
17
20
* MSCI World, JPM Global (total return index)

Earning reporting season from Q1

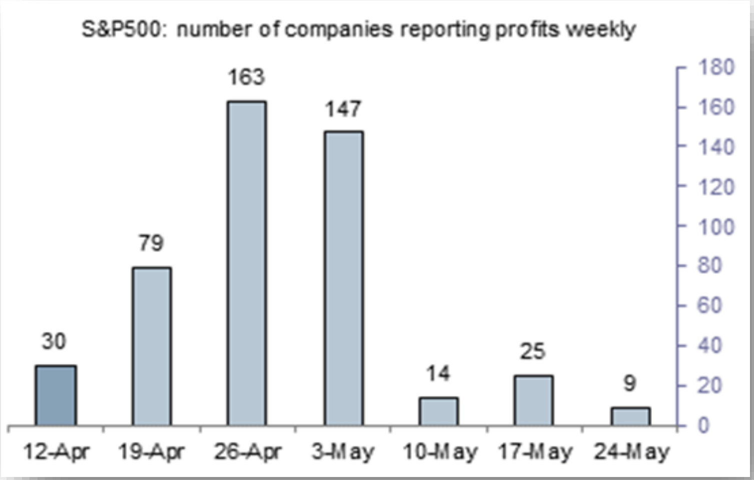
In mid-April central banks will begin communication for US business earnings from the 1st quarter, which will then truly begin at the end of the month.

Analysts, during the 1st quarter, raised again estimates on earnings growth to a yearly 24%. Estimates are amplified by the comparison with an already weak 1st quarter in 2020, but the trimestral variance, close to 3%, appears to be anything but excessive, considering the positive course of macro data. The same estimates on GDP started at 2.5% by the end of 2020, to get to the actual 5.3%.

Usually, estimates are cut down as results are being published. This is instead the third consecutive trimester in which estimates are positively revised in the quarter preceding the reporting season. It’s an element to focus on, which also reflects the overly-aggressive estimate cuts in the spring of 2020 and how they have never been regained, as clearly shown by the fact that esteems have always been exceeded by the good business results from previous quarters. Finally, expectations on the results as expressed by firms resulted more optimistic than expected.

At sectorial level, the major reviews regarded energy and raw materials industry, following the upward push by oil and raw materials prices, while the increase in rates caused estimates on financial products to be reviewed, highlighting a prevalence of cyclic themes.

On historical average the yearly net results exceeded the expectations from the beginning of the season by 4%. During the last three seasons the average exceeding is around 14%. Imagining a surprise effect following the historical average we’d see a 28% increase in earnings, the highest since 2010.


S&P500: number of companies reporting profits weekly
30
79
163
147
14
25
9
12-Apr
19-Apr
26-Apr
3-May
10-May
17-May
24-May
180
160
140
120
100
80
60
40
20
0

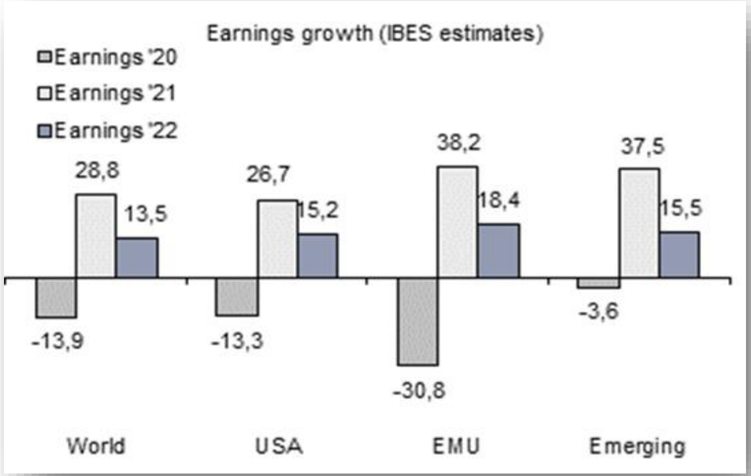

Earnings growth 12 months forward (IBES)
% yoy
Topix
Eurostoxx
Emergenti
S&P500
50
46
42
38
34
30
26
22
18
14
10
6
2
-2
-6
-10
18
19
20
21

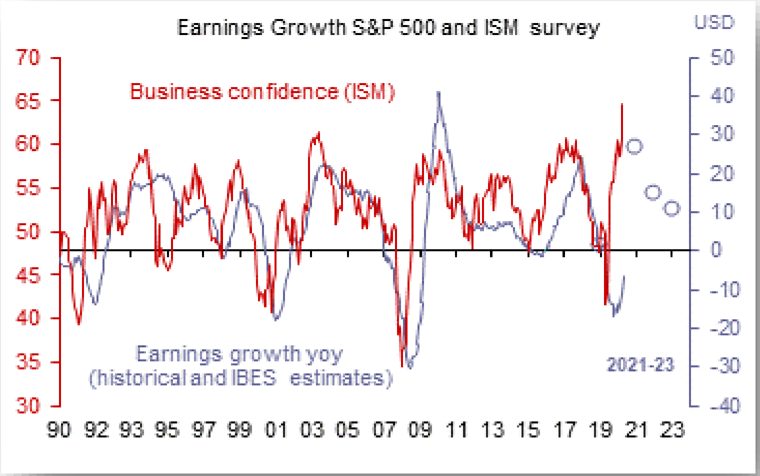
Estimates on the medium-term

In addition to the 1st quarter's esteems, analysts positively reviewed expectations for the whole of 2021 for the US, with a +5% increase, second only to the one registered in the first 3 months of 2018, when the profit taxation reform took place.

After 2020's contraction, analysts forecast a strong earnings growth in 2021, which would intensify over the central quarters of the year, thanks to the success of vaccinations. Estimates see earnings growing by almost 27% for S&P500 firms, above 35% for Eurostoxx and emerging countries.

These are exceptional numbers in absolute value, but those in turn will correct the record contraction from 2020. In addition, earnings growth will find support in a macro-recovery expected to take place in the central months of the year, when the effects of fiscal stimuluses and business reopening will cumulate. Earnings recovery is expected to then continue strongly in 2022, but with a less intense pace.

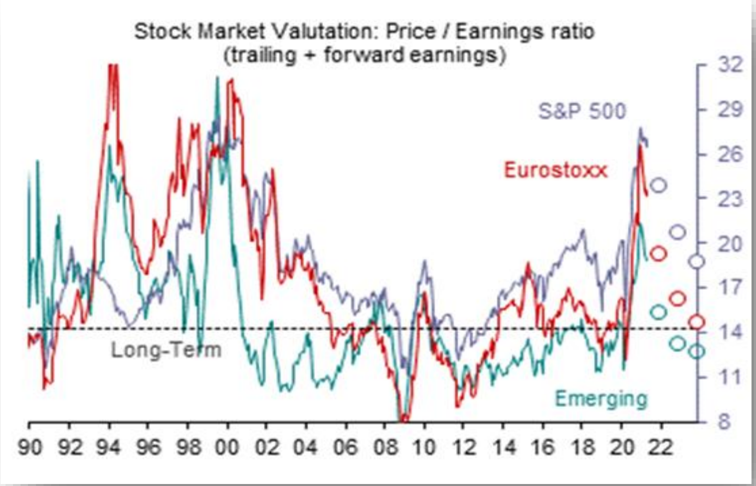

Earnings growth (IBES estimates)
Earnings '20
Earnings '21
Earnings '22
28,8
13,5
-13,9
26,7
15,2
-13,3
38,2
18,4
-30,8
37,5
15,5
-3,6
World
USA
EMU
Emerging

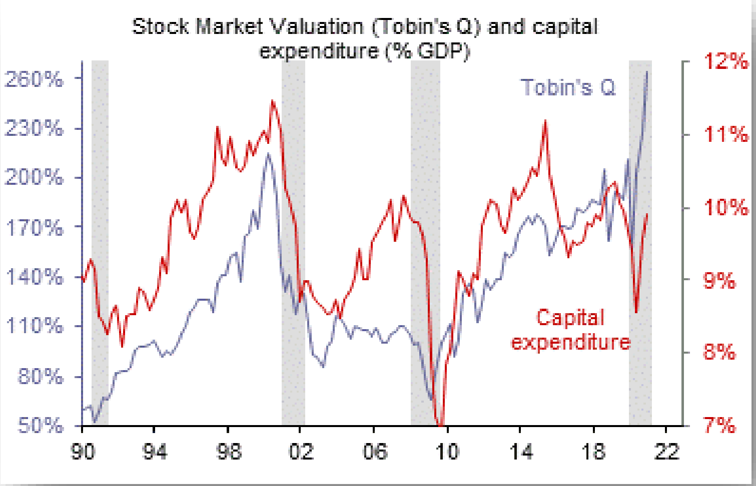

Earnings Growth S&P 500 and ISM survey
USD
Business confidence (ISM)
Earnings growth yoy
(historical and IBES estimates)
2021-23
70
65
60
55
50
45
40
35
30
50
40
30
20
10
0
-10
-20
-30
-40
90 92 93 95 97 99 01 03 05 07 09 11 13 15 17 19 21 23

Stock markets: from profits growth to investments increasing

Stock markets received well the normalization of US rates, thanks to the support from the new profits growth. The guiding element for stocks, in the absence of help from multiples (already on high levels), will essentially be the acceleration of profits. The balance between profits and rates will be paramount to allow the upward trend by the stock to continue.

In addition to the cyclic recovery, conditions for the strengthening of long-term growth are being created. After 2008's recession, support for recovery essentially came from monetary policies. The uncertainty of a slow recovery (given the lack of fiscal stimuluses), high private debt and low multiples made it easier for firms to distribute dividends in the long run and to make buybacks rather than investments. The joint usage of monetary and fiscal policies in 2020, high multiples (which make buybacks more expensive) and low rates could induce firms to increase investment amounts and productive capacity, with a succeeding improvement of productivity on the long-term. This virtuous cycle, the increase in consumption, profits growth, higher employment and investments would all be supported by the infrastructural and environmental investment plan by the US' new administration.


Stock Market Valutation: Price / Earnings ratio
(trailing + forward earnings)
S&P 500
Eurostoxx
Long-Term
Emerging
32
29
26
23
20
17
14
11
8
90 92 94 96 98 00 02 04 06 08 10 12 14 16 18 20 22


Stock Market Valuation (Tobin's Q) and capital
expenditure (% GDP)
Tobin's Q
Capital
expenditure
260%
230%
200%
170%
140%
110%
80%
50%
12%
11%
10%
9%
8%
7%
90 94 98 02 06 10 14 18 22