STRATEGY NOTES: The recovery of earnings continues, but its pace is normalising after the acceleration seen in the first half of 2021.

19h January 2022

The 4Q 2021 corporate earnings reporting season opened in the United States in mid-January (and will be followed by the European round of results at the end of the month).
The recovery of earnings continues, but its pace is normalising after the acceleration seen in the first half of 2021.
In the United States earnings growth is forecast at around 21% y/y (from 37% the previous quarter), although the quarterly change should prove slightly negative. Revenues are expected to continue showing solid growth, by 12% y/y (from 17% the previous quarter). In the Eurozone, earnings growth is forecast at +12% y/y.

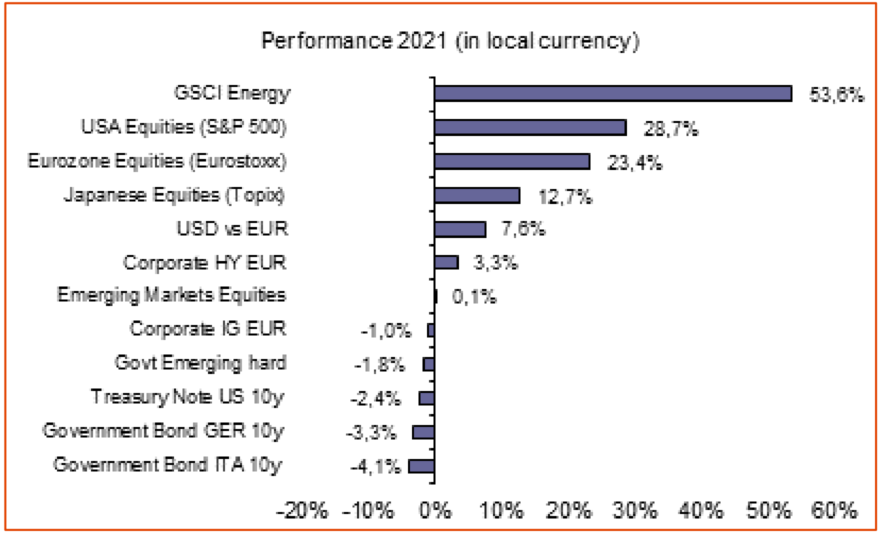
The earnings season will also be in the spotlight to verify the evolution of profit margins (in light of higher cost of labour and of the normalisation of the recovery) from peak levels, as well as the guidance on earnings in the present quarter, that will be temporarily impacted by the Omicron variant.

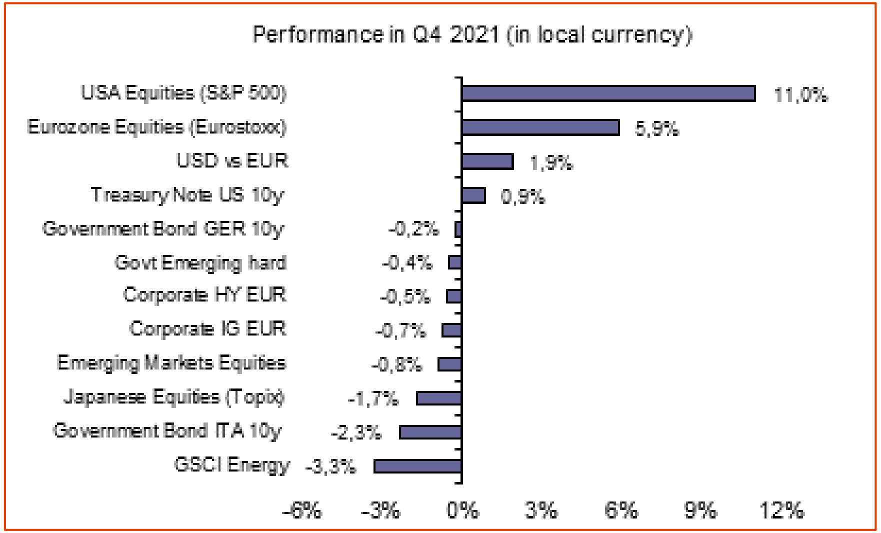
MARKET PERFORMANCES IN 4Q 2021 AND 2021

In the course of 4Q, the major global stock markets continued to post excellent performances. The upswing was driven by the US stock index, that rose to new all-time on expectations for a strengthening of economic growth. The Eurozone stock markets followed at a distance, as the recovery in Europe is on track but slower, due to the higher rate of Covid cases.

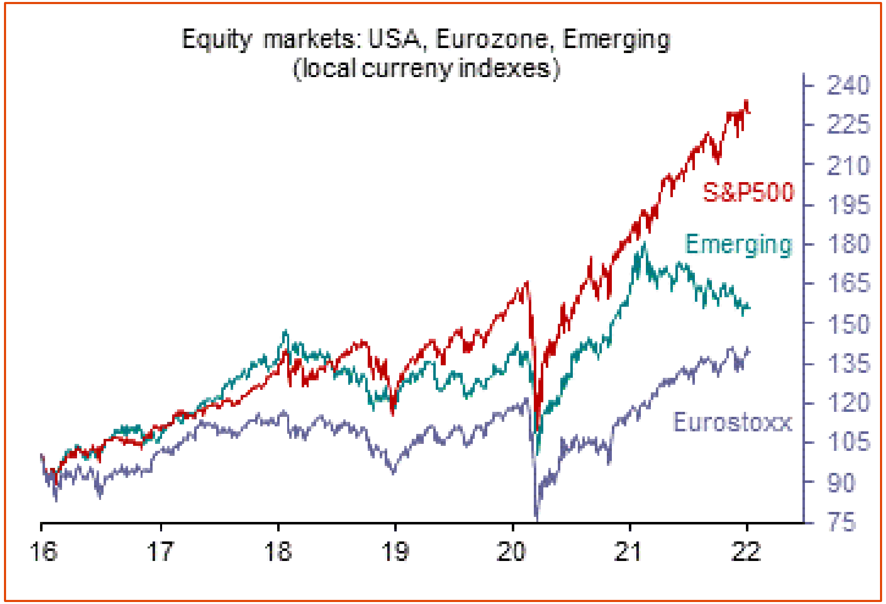
Results for 2021 as a whole are proving markedly positive in the advanced countries, as opposed to marginally negative earnings in the emerging markets, affected by the slowdown of China. Government bonds performed negatively in nominal terms and even more so in real terms. Yields rose to close to pre-Covid levels, in a context of ongoing economic recovery, driven by up inflation, as the central banks prepare to taper the emergency measures introduced to counter the pandemic. The performance of High Yield bonds was positive, but stopped slightly short of coupon rates.

MARKET PERFORMANCES IN 4Q 2021 AND 2021





MARKET PERFORMANCES IN 4Q 2021 AND 2021



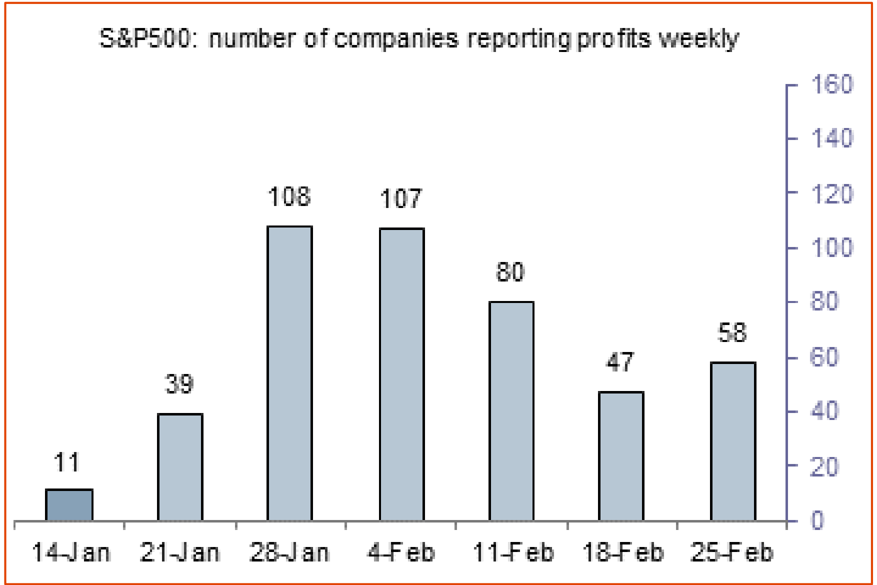
4Q 2021 EARNINGS REPORTING SEASON

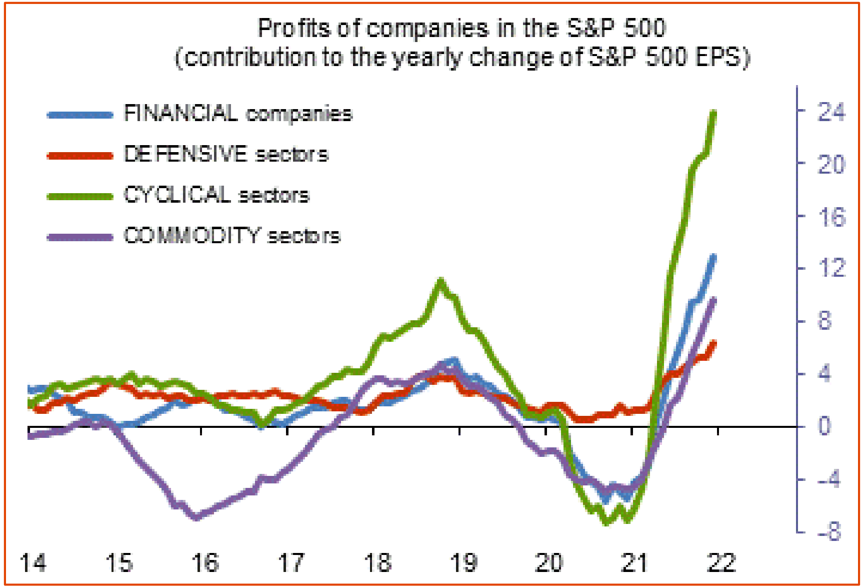
In the United States, the country's major banks kicked off the round of 4Q corporate earnings reports, that will be at its most intense at the end of January (when European companies will also report their results).

Analysts expect solid earnings growth on the US stock market, by around 20% y/y, from 37% in 3Q 2021. Quarterly growth is expected in negative territory, on the other hand (by close to -4%). Earnings growth should be driven by the cyclical sectors, and in particular by energy, basic materials, and industrials, followed by pharmaceuticals and technology.

Analysts kept earnings forecasts essentially stable in the run-up to the reporting season. This marks a further step in the return to normal of forecasts as well, typically cautious in the pre-pandemic period (as opposed to the sharp upside revisions of forecasts seen in the period following the spring 2020 crash).
Expectations for declining earnings in the quarter, and cautious forecasts, diverge from a strengthening macro picture in 4Q. This could result in major upside surprises from earnings (albeit not to the exceptional extent seen during the pandemic).

4Q 2021 EARNINGS REPORTING SEASON





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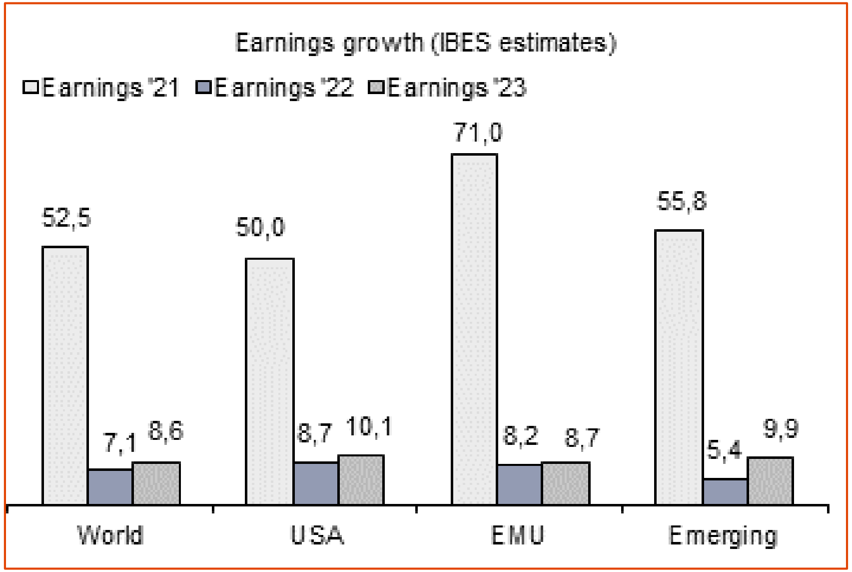
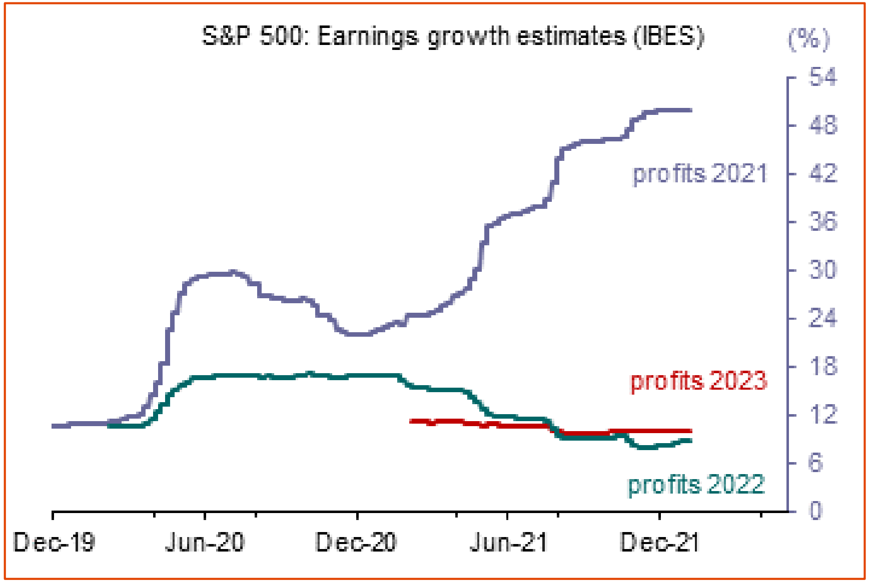
MEDIUM-TERM FORECASTS

Earnings growth, after flaring up in 2021 (+50% for the S&P500, +70% for the Eurostoxx), is expected to return to levels in line with long-term averages (8%-10% for the advanced markets) this year.
This seems consistent with a slowdown of economic growth in 2022, after the acceleration boosted by reopenings in 2021, marking a new step in the return to “normal”.
Earnings growth is forecast at the same levels in 2023 as well.

In the Emerging Markets, earnings growth in 2022 is expected to prove weaker than in the advanced countries. The Asian and Latin American countries are feeling the long wave of the pandemic, ongoing disruptions to global trade and the resulting impact on inflation, that local central banks have already attempted to counter by tightening their monetary policies. Earnings growth is forecast stronger in 2023.

MEDIUM-TERM FORECASTS





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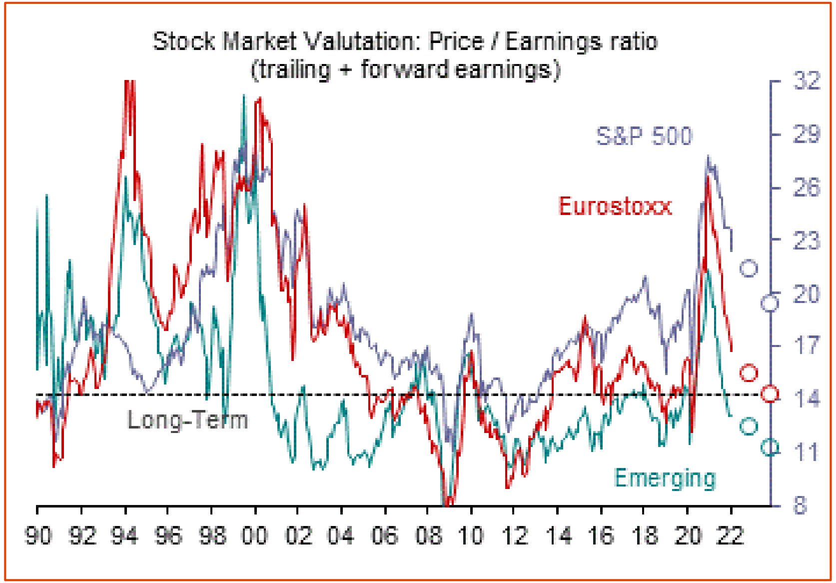
VALUATION EXCESSES EASING, FOCUS ON EARNINGS

The earnings reporting season kicks of with market **valuations that have reabsorbed in part the excesses seen in the opening months of 2021**. Multiples (Price/Earnings) have dropped as prices rose less than earnings.
The re-absorption of valuation excesses is more evident in the Emerging Markets and on the Eurostoxx. Valuations remain richer on the S&P500 index, where high-growth sectors such as technology have reported more stable multiples.
As a result, **the risk premium has increased further**, with return from corporate earnings exceeding bond yields by far.
Over the past 20 months, the uninterrupted upswing of the stock markets has been supported by the ample liquidity made available by the central banks, and by accelerating earnings.
In 2022, the removal of monetary stimulus may result in bouts of volatility on the markets, while the normalisation of the recovery will shift focus from macro themes to earnings growth, and selectivity among sectors and individual securities will become more important.

VALUATION EXCESSES EASING, FOCUS ON EARNINGS



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