Multi Asset
Macro Views

UNIGESTION

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That Don't Impress Me Much – Shania Twain, 1997

Q3 EARNINGS PROVIDE CAUSE FOR OPTIMISM DESPITE FAILING TO IMPRESS INVESTORS

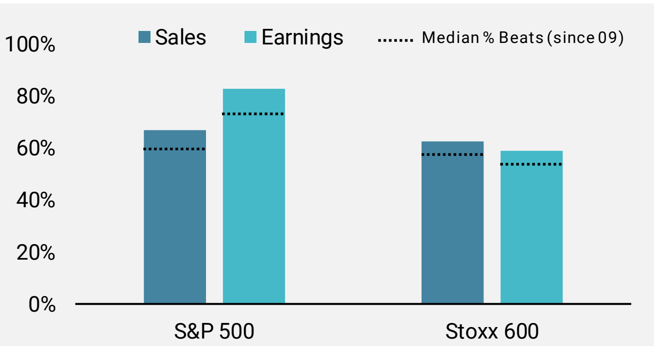
The Q3 earnings season is coming to a close and has thus far proceeded in much the same way as recent quarters: muted expectations from analysts have been surpassed by firms' results. While equity markets continued to move higher, the performance gap between firms beating versus missing their estimates suggests investors were less impressed by the results. Looking ahead, supply chain challenges and labour shortages are likely to persist for some time, but with firms putting capital to use, primarily via share repurchases, the context for equity markets remains positive in our view.

WHAT HAPPENED?

Firms continue to post strong results…

The bulk of firms in the US and Europe have now reported their results for Q3, and they have been fairly strong: based on the 73% of firms in the S&P 500 that have reported so far, 83% are beating their Q3 earnings estimates and 67% are beating their sales estimates. For the 62% of Stoxx 600 firms reporting, 59% are beating their earnings consensus estimates and 63% are beating on sales. In year-over-year terms, sales are up 18.5% and earnings 39.4% for reporting firms in the S&P 500, while Stoxx 600 firms are seeing 14.3% sales growth and 44.3% earnings growth.

Figure 1: Percentage of Firms Beating Estimates



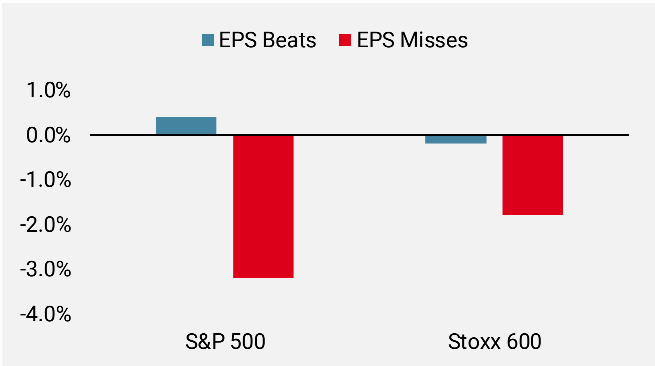
Source: Bloomberg, JPM, Unigestion, as of 3 November 2021.

The strong results are also broad-based, at least in the US: the Utilities sector in the S&P 500 has been the laggard in surprises thus far, and 60% of these firms are still beating their earnings estimates. At the other end, over 90% of Technology firms have beat on earnings. In Europe, there is greater variation across sectors, with just 38% of Consumer Discretionary firms beating their earnings estimates while 81% of Financials are beating theirs.

…yet investors are not impressed

Overall, equity markets have rallied further this earnings season, with the S&P 500 up 6% and the Stoxx 600 up 4% since the first day of reporting to ahead of the Fed meeting and press conference last Wednesday. However, market action suggests investors have not been so impressed by the results and other drivers are pushing equity markets higher. Figure 2 compares the median 1-day price return (relative to the market) of firms that beat their EPS estimates versus those that missed for the S&P 500 and Stoxx 600. As the chart shows, firms who beat estimates were not rewarded nearly to the same degree that firms missing were punished. This asymmetry suggests that investors were likely more optimistic than analysts.

Figure 2: Median 1-day Performance versus Market



Source: JPM, Unigestion, as of 3 November 2021.

Bottlenecks very much the focus of company commentary

One of the key topics this earnings season was the impact of supply chain disruptions and labour shortages. Few firms escaped these headwinds, and indeed many expect them to continue into the next quarter and, in some cases, next year. Figure 3 highlights a few notable comments from firms during this earnings season.

Figure 3: Company Comments on Labour/Supply

Company	Comment
Apple	Estimates supply headwinds cost USD 6bn in Q3, worsening for iPhone and extending to iPad
Intel	Q3 results hit by supply constraints and conservative 2022 outlook due to ongoing supply chain constraints
Amazon	Expects supply chain and labour issues to cost USD 4bn in Q4
Facebook	Noted supply and labour shortages weighing on sales
Northrop Grumman	Cited "labor and supply chain challenges" in their sales miss
Lockheed Martin	Noted supply chain hit on 2021 and expected 2022 sales
Nike	Lowered guidance due to supply chain uncertainties
McCormick	Cut profit outlook due to supply chain issues
Kimberly-Clark	Cut annual forecast due to supply chain disruptions and inflationary pressures
Lennar	Noted that "during the third quarter, our company and the homebuilding industry as a whole continued to experience unprecedented supply chain challenges which we believe will continue into the foreseeable future."

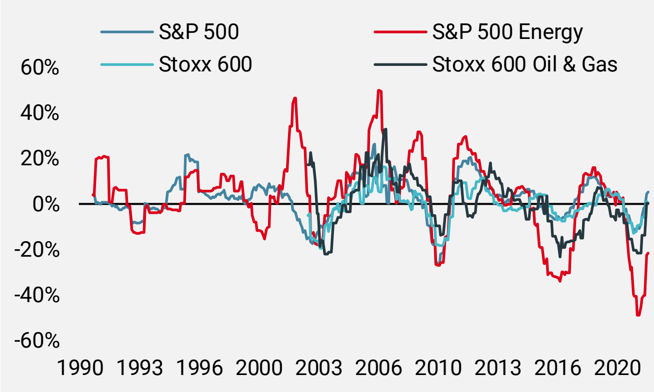
Source: JPM, Unigestion, as of 3 November 2021.

While there are a few different paths through which these bottlenecks may be resolved (declining demand, additional capacity being brought online, delivery delays), they will likely persist into the rest of this year and part of next year as well.

Firms are starting to put capital to work

After becoming flush with cash in the immediate aftermath of the coronavirus crisis, firms have started to put that capital to use. Indeed, among non-financial firms in the S&P 500 that have reported thus far, their cash balances have remained stable quarter-over-quarter and are down -3% year-over-year. One important use of cash has been capital expenditures, which are now in aggregate growing for the S&P 500 and Stoxx 600 and improving for the Energy/Oil & Gas sectors, which have seen some of the largest cuts in capex over the last few years (see Figure 4). A continuation of this trend would provide a key support to growth.

Figure 4: Year-over-year Capex Growth



Source: Bloomberg, Unigestion, as of 3 November 2021.

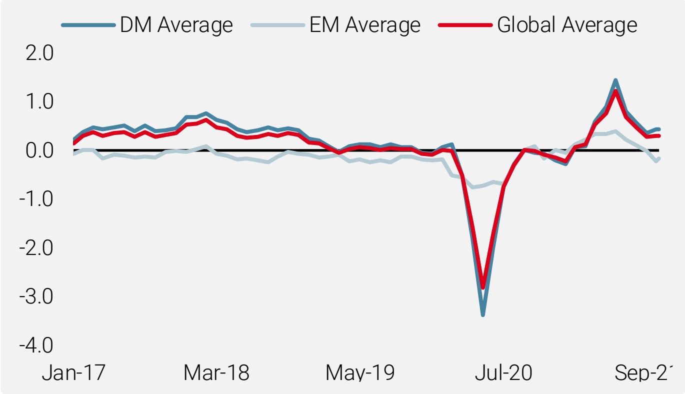
However, capex is not the only use of cash that is seeing significant growth. Buybacks for S&P 500 firms reporting thus far are up 13% quarter-over-quarter and 68% year-over-year (vs 7% and 20%, respectively, for capex). More than 80% of the share repurchases have been funded with cash, and over USD 730bn worth of buybacks have been announced this year, eclipsing the 2019 level of USD 702bn and approaching the massive USD 939bn seen in 2018.

A positive context for equity risk

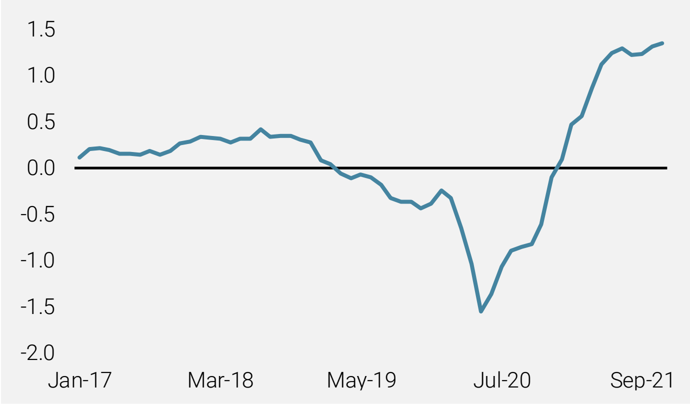
Earnings season has largely confirmed our expectations: firm revenue and profitability remain very strong, and though supply/labour bottlenecks are likely to continue to be a drag for the foreseeable future, healthy demand provides sufficient support to equity markets. The Fed meeting last Wednesday also confirmed that the world's key central bank will remain patient and continue to provide ample liquidity to markets until the middle of next year. Interest rate lift-off is still some time away with "still ground to cover to reach maximum employment." Thus we believe the context for equity risk going into the rest of the year has improved significantly following this earnings season and a supportive Fed meeting.

UNIGESTION NOWCASTING

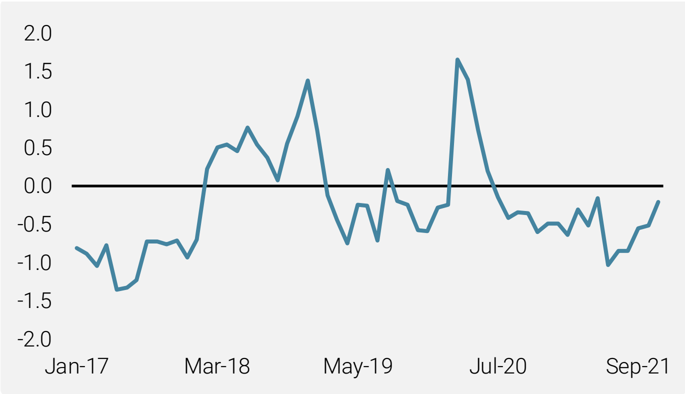
World Growth Nowcaster



World Inflation Nowcaster



Market Stress Nowcaster



Weekly Change

- Last week, our World Growth Nowcaster was steady as better data from China was offset by a deterioration in Australia.
- Our World Inflation Nowcaster moved slightly higher driven largely by higher readings out of Europe and China.
- Our Market Stress Nowcaster moved modestly higher as liquidity indicators became less supportive.

Sources: Unigestion, Bloomberg, as of 5 November 2021.

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