

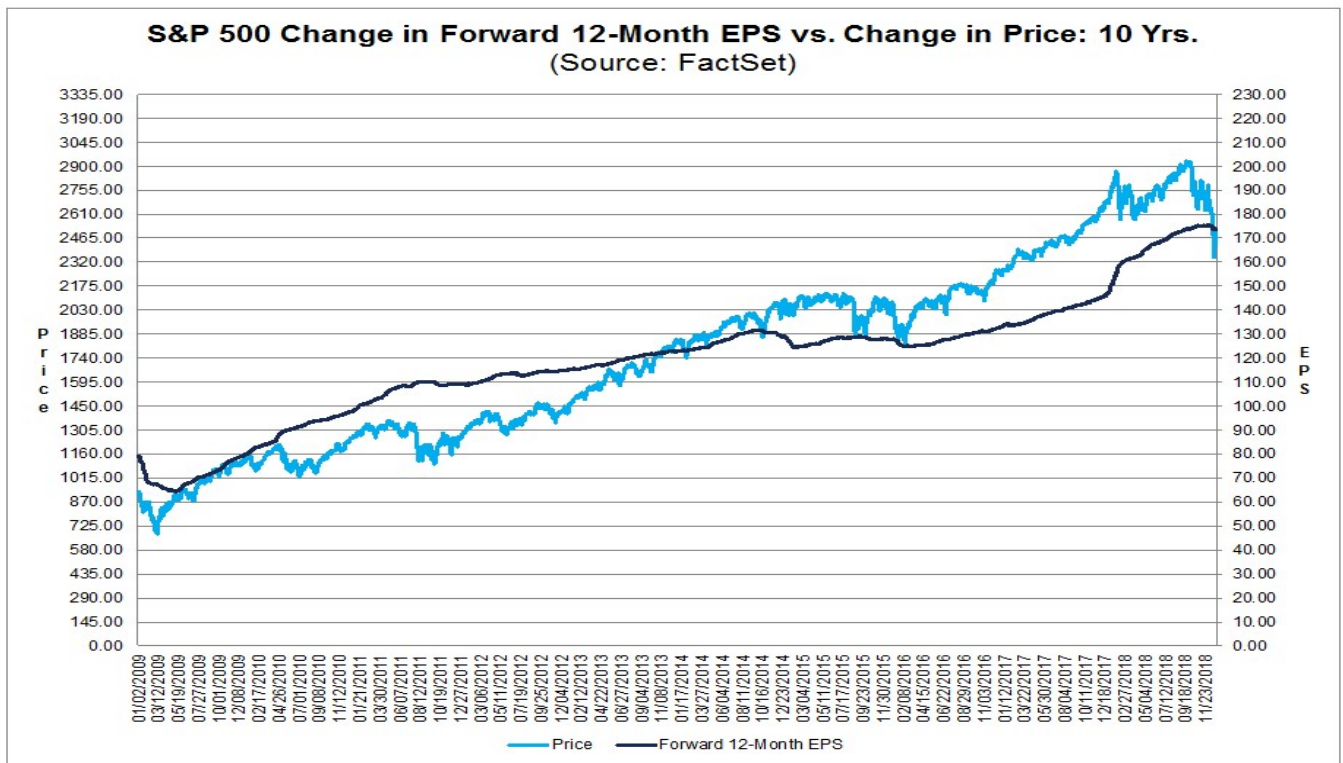
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January 4, 2019

Key Metrics

- **Earnings Growth:** For Q4 2018, the estimated earnings growth rate for the S&P 500 is 11.4%. If 11.4% is the actual growth rate for the quarter, it will mark the fifth straight quarter of double-digit earnings growth for the index.
- **Earnings Revisions:** On September 30, the estimated earnings growth rate for Q4 2018 was 16.7%. All eleven sectors have lower growth rates today (compared to September 30) due to downward revisions to EPS estimates.
- **Earnings Guidance:** For Q4 2018, 72 S&P 500 companies have issued negative EPS guidance and 33 S&P 500 companies have issued positive EPS guidance.
- **Valuation:** The forward 12-month P/E ratio for the S&P 500 is 14.1. This P/E ratio is below the 5-year average (16.4) and below the 10-year average (14.6).
- **Earnings Scorecard:** For Q4 2018 (with 4% of the companies in the S&P 500 reporting actual results for the quarter), 89% of S&P 500 companies have reported a positive EPS surprise and 67% have reported a positive sales surprise.



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Topic of the Week: 1

Largest Cuts to Quarterly S&P 500 EPS Estimates Since Q3 2017

During the fourth quarter, analysts lowered earnings estimates for companies in the S&P 500 for the quarter. The Q4 bottom-up EPS estimate (which is an aggregation of the median EPS estimates of all the companies in the index) dropped by 3.8% (to \$40.93 from \$42.56) during this period. How significant is a 3.8% decline in the bottom-up EPS estimate during a quarter? How does this decrease compare to recent quarters?

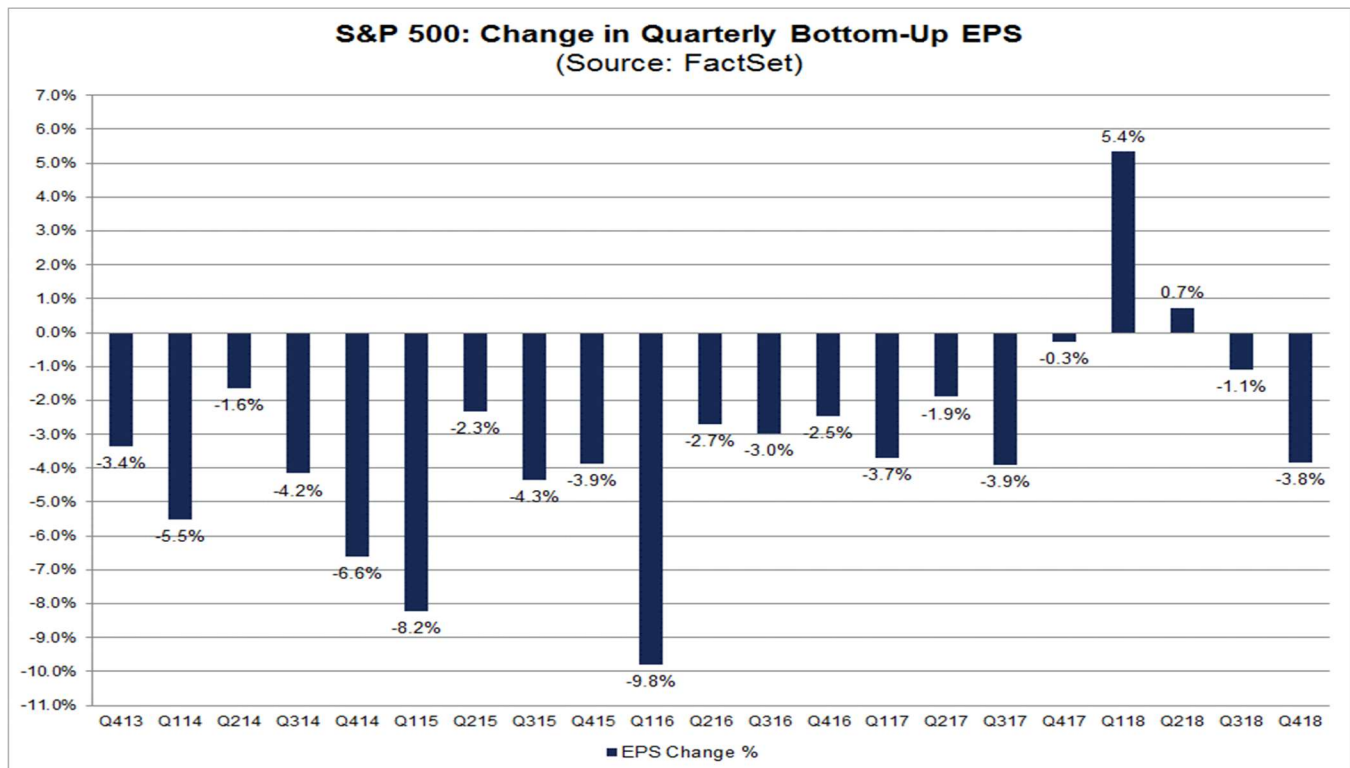
Over the past five years (20 quarters), the average decline in the bottom-up EPS estimate during a quarter has been 3.1%. Over the past ten years, (40 quarters), the average decline in the bottom-up EPS estimate during a quarter has been 4.5%. Over the past fifteen years, (60 quarters), the average decline in the bottom-up EPS estimate during a quarter has been 3.9%. Thus, the decline in the bottom-up EPS estimate recorded during the fourth quarter was larger than the 5-year average, but smaller than the 10-year average and the 15-year average.

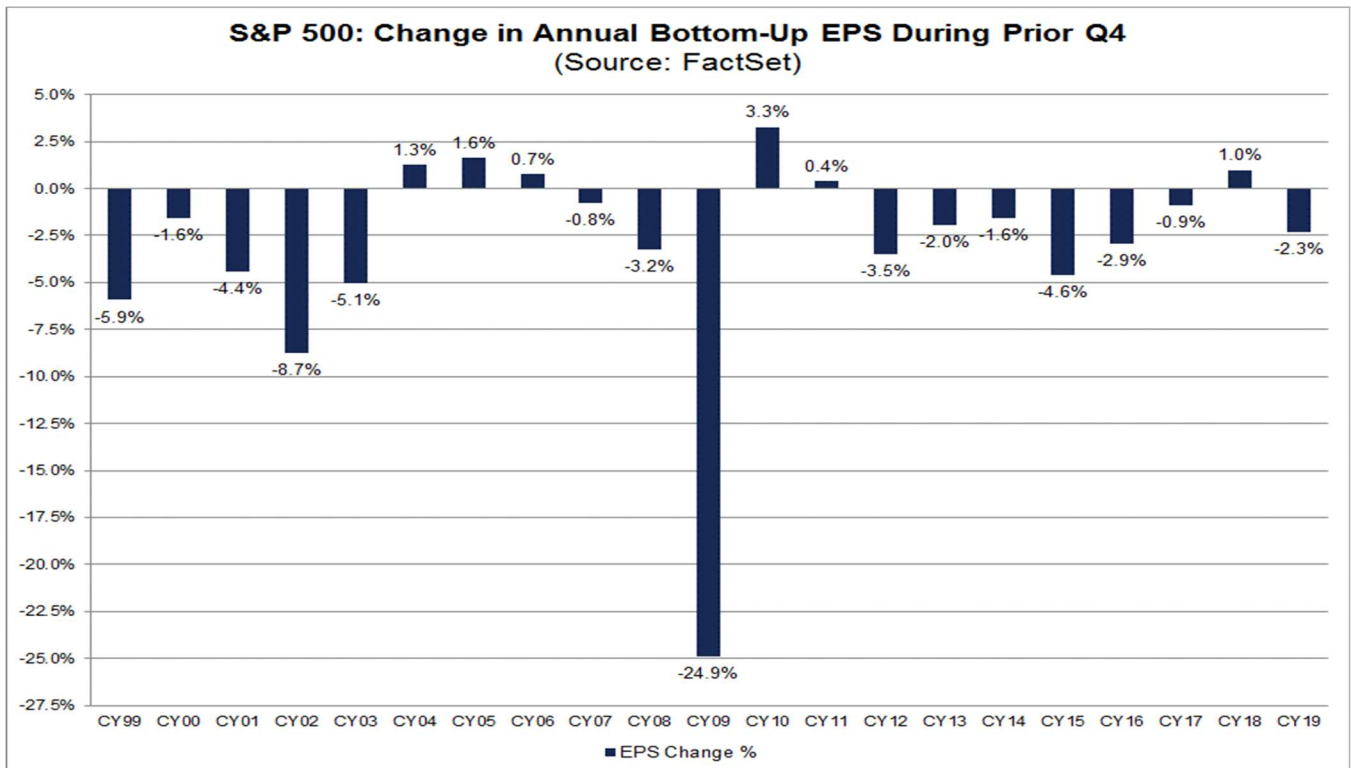
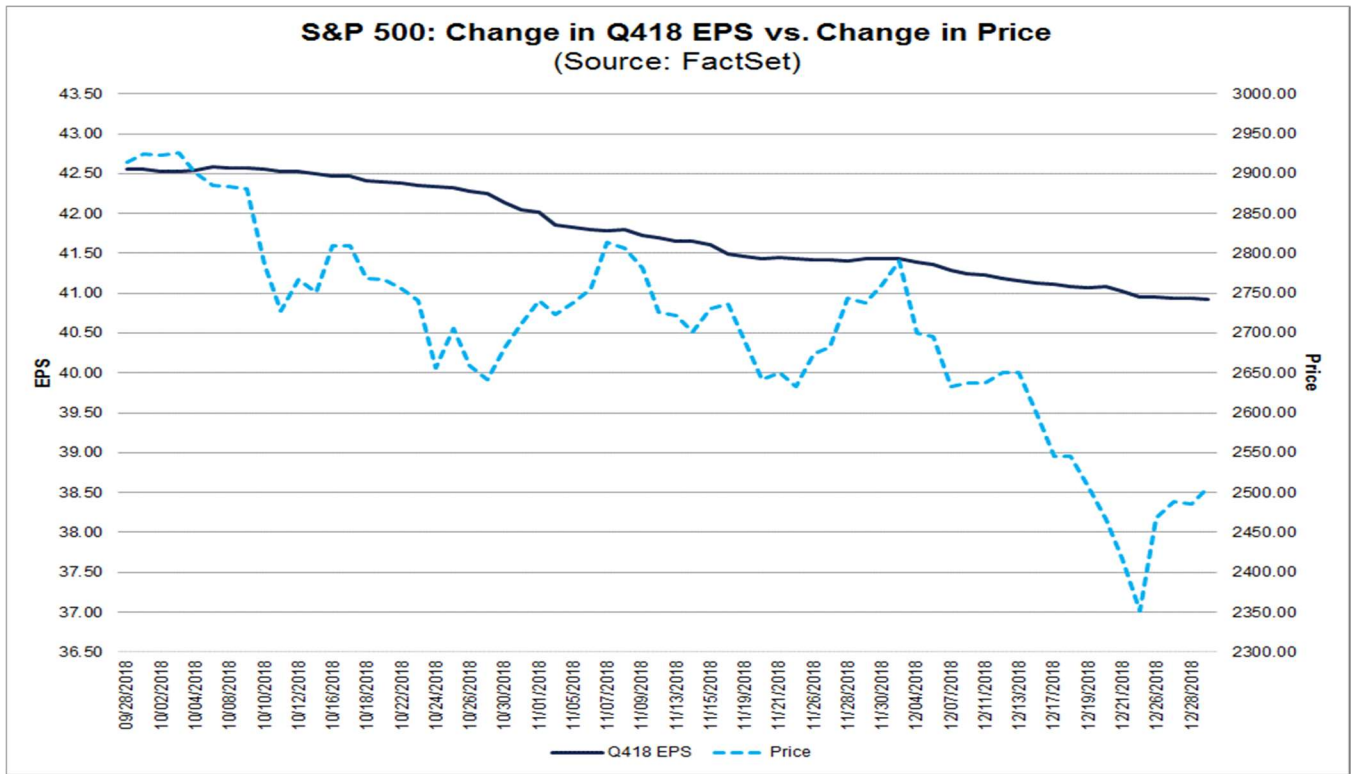
However, the fourth quarter did mark the largest percentage decline in the bottom-up EPS estimate during a quarter since Q3 2017 (-3.9%).

At the sector level, all eleven sectors recorded a decline in their bottom-up EPS estimate during the quarter, led by the Materials (-9.5%), Utilities (-8.9%), and Energy (-7.3%) sectors.

As the bottom-up EPS estimate for the index declined during the quarter, the value of the S&P 500 also decreased during this same period. From September 30 through December 31, the value of the index decreased by 14.0% (to 2506.85 from 2913.98). The fourth quarter marked just the third time in the past 20 quarters in which the both bottom-up EPS estimate and value of the index decreased during the quarter.

It is interesting to note that the bottom-up EPS estimate for CY 2019 decreased by 2.3% (to \$173.94 from \$178.05) during the fourth quarter. This decline was larger than the 5-year average (-1.8%) decrease in the annual bottom-up EPS estimate during the fourth quarter, but smaller than the 10-year (-3.6%), 15-year (-2.4%) and 20-year (-3.1%) average decreases in the annual bottom-up EPS estimate during the fourth quarter.





Topic of the Week: 2

S&P 500 Likely to Report Earnings Growth Above 15% in Q4 2018

As of today, the S&P 500 is expected to report earnings growth of 11.4% for the fourth quarter. What is the likelihood the index will report an actual earnings increase of 11.4% for the quarter?

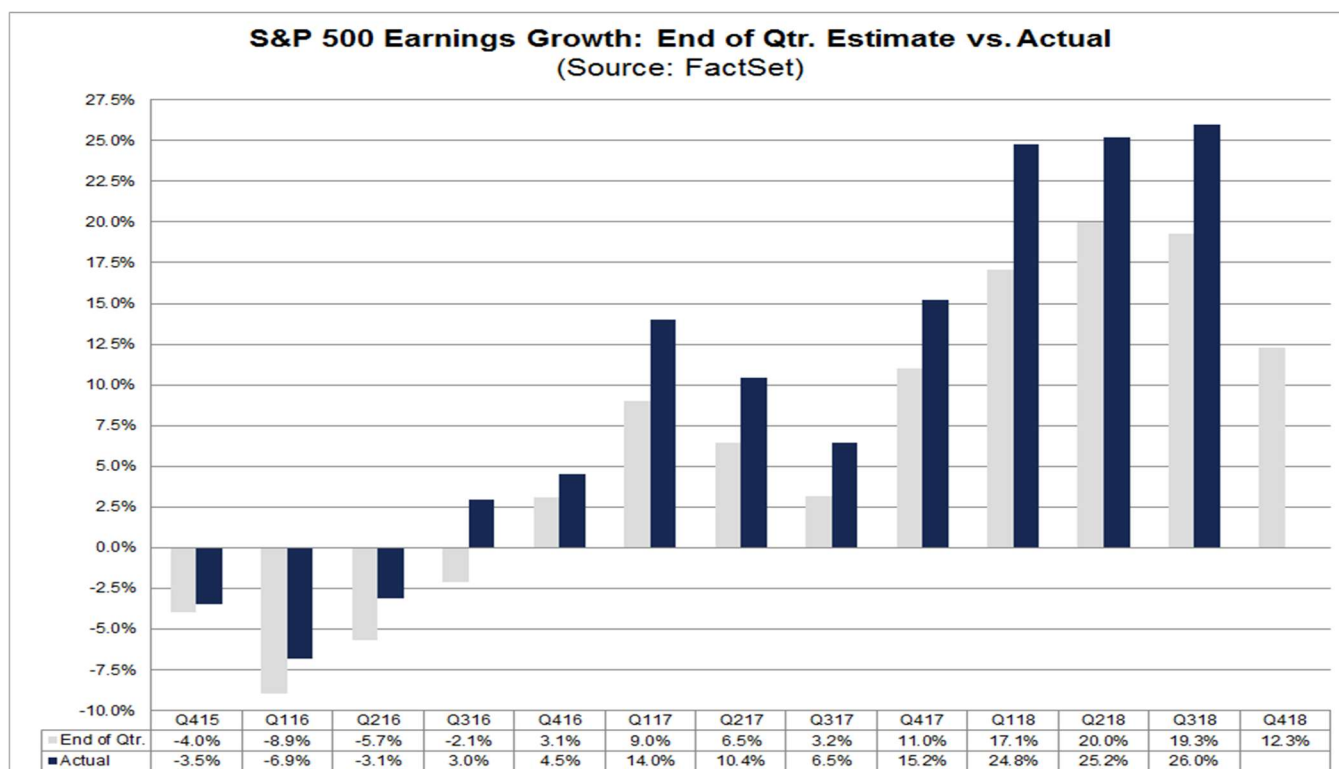
Based on the average change in earnings growth due to companies reporting positive earnings surprises, it is likely the index will report earnings growth above 15% for Q4, but below the 25% growth reported in the previous three quarters.

When companies in the S&P 500 report actual earnings above estimates during an earnings season, the overall earnings growth rate for the index increases because the higher actual EPS numbers replace the lower estimated EPS numbers in the calculation of the growth rate. For example, if a company is projected to report EPS of \$1.05 compared to year-ago EPS of \$1.00, the company is projected to report earnings growth of 5%. If the company reports actual EPS of \$1.10 (a \$0.05 upside earnings surprise compared to the estimate), the actual earnings growth for the company for the quarter is now 10%, five percentage points above the estimated growth rate (10% - 5% = 5%).

Over the past five years on average, actual earnings reported by S&P 500 companies have exceeded estimated earnings by 4.8%. During this same period, 71% of companies in the S&P 500 have reported actual EPS above the mean EPS estimate on average. As a result, from the end of the quarter through the end of the earnings season, the earnings growth rate has typically increased by 3.8 percentage points on average (over the past 5 years) due to the number and magnitude of upside earnings surprises.

If this average increase is applied to the estimated earnings growth rate at the end of Q4 (December 31) of 12.3%, the actual earnings growth rate for the quarter would be 16.1% (12.3% + 3.8% = 16.1%).

If the index does report growth of 16.1% for Q4 2018, it will mark the first time the index has not reported earnings growth above 20% since Q4 2017. However, it will mark the fifth straight quarter of double-digit earnings growth for the index.



Q4 Earnings Season: By The Numbers

Overview

In terms of estimate revisions for companies in the S&P 500, analysts reduced EPS estimates within average levels for Q4 2018. On a per-share basis, estimated earnings for the fourth quarter fell by 3.8% during the quarter. This percentage decline was larger than the 5-year average (-3.1%) for a quarter, but smaller than the 10-year average (-4.5%) and the 15-year average (-3.9%) for this period.

In addition, an average number of S&P 500 companies have lowered the bar for earnings for Q4 2018 relative to recent quarters. Of the 105 companies that have issued EPS guidance for the fourth quarter, 72 have issued negative EPS guidance and 33 have issued positive EPS guidance. The percentage of companies issuing negative EPS guidance is 69% (72 out of 105), which is slightly below the 5-year average of 70%.

Because of the net downward revisions to earnings estimates, the estimated year-over-year earnings growth rate for Q4 2018 has decreased to 11.4% today from 16.7% on September 30. Ten of the eleven sectors are predicted to report year-over-year earnings growth. Six sectors are projected to report double-digit growth in earnings for the quarter, led by the Energy, Industrials, Financials, and Communication Services sectors.

Because of the net downward revisions to revenue estimates, the estimated year-over-year revenue growth rate for Q4 2018 has decreased to 6.1% today from 6.9% on September 30. Ten of the eleven sectors are projected to report year-over-year growth in revenues. Four sectors are predicted to report double-digit growth in revenues: Communication Services, Energy, Real Estate, and Materials.

Looking at future quarters, analysts see single-digit earnings growth for the first three quarters of 2019.

The forward 12-month P/E ratio is 14.1, which is below the 5-year average and below the 10-year average.

During the upcoming week, two S&P 500 companies are scheduled to report results for the fourth quarter.

Earnings Revisions: Largest Decline in Energy Sector

Decline in Estimated Earnings Growth Rate for Q4 This Week Due to Apple

The estimated earnings growth rate for the fourth quarter is 11.4% this week, which is below the estimated earnings growth rate of 12.4% last week. Downward revisions to estimates for Apple were mainly responsible for the decrease in the overall growth rate during the week, as the company issued revenue guidance for Q4 2018 on Wednesday that was below the mean revenue estimate. As a result, the mean EPS estimate for Apple for Q4 2018 decreased to \$4.21 from \$4.66 during the week.

The estimated earnings growth rate for the S&P 500 for Q4 2018 of 11.4% today is below the estimated earnings growth rate of 16.7% at the start of the quarter (September 30). All eleven sectors have a recorded a decrease in expected earnings growth due to downward revisions to earnings estimates, led by the Energy, Utilities, and Materials sectors.

Energy: Exxon Mobil and Chevron Lead Decline

The Energy sector has recorded the largest decrease in expected earnings growth since the start of the quarter (to 74.6% from 95.4%). This sector has also witnessed the largest decrease in price since September 30 at -23.7%. Overall, 19 of the 30 companies (63%) in the Energy sector have seen a decrease in their mean EPS estimate during this time. Of these 19 companies, 14 have recorded a decrease in their mean EPS estimate of more than 10%, led by Hess Corporation (to -\$0.09 from \$0.10), National Oilwell Varco (to \$0.08 from \$0.16) and Valero Energy (to \$0.93 from \$1.50). However, Exxon Mobil (to \$1.11 from \$1.36) and Chevron (to \$1.95 from \$2.25) have been the largest contributors to the decrease in earnings for this sector during this period. The stock prices for both Exxon Mobil (-17.6%) and Chevron (-9.7%) have declined since September 30.

Utilities: 86% of Companies Have Seen a Decline in Earnings Estimates

The Utilities sector has recorded the second largest decrease in expected earnings growth since the start of the quarter (to -5.3% from 10.2%). Despite the decline in expected earnings, this sector has witnessed the smallest decrease in price since September 30 at -1.2%. Overall, 25 of the 29 companies (86%) in the Utilities sector have seen a decrease in their mean EPS estimate during this time. Of these 25 companies, 10 have recorded a decrease in their mean EPS estimate of more than 10%, led by Entergy, (to \$0.34 from \$0.86), NRG Energy (to \$0.15 from \$0.28), Evergy (to \$0.21 from \$0.35), and Pinnacle West Capital (to \$0.18 from \$0.30). The stock prices of all four of these companies have increased since September 30.

Materials: 80% of Companies Have Seen a Decline in Earnings Estimates

The Materials sector has recorded the third largest decrease in expected earnings growth since the start of the quarter (to 9.3% from 17.6%). This sector has also witnessed a decrease in price of 14.8% since September 30. Overall, 20 of the 25 companies (80%) in the Materials sector have seen a decrease in their mean EPS estimate during this time. Of these 20 companies, 7 have recorded a decrease in their mean EPS estimate of more than 10%, led by Freeport McMoRan (to \$0.21 from \$0.33), Martin Marietta Materials, (to \$1.84 from \$2.58), WestRock Company (to \$0.84 from \$1.13), and Newmont Mining (to \$0.25 from \$0.33).

Index-Level (Bottom-Up) EPS Estimate: Average Decline in Q4

The Q4 bottom-up EPS estimate (which is an aggregation of the median earnings estimates for all 500 companies in the index and can be used as a proxy for the earnings for the index) decreased by 3.8% (to \$40.93 from \$42.56) during the fourth quarter. This percentage decline was larger than the 5-year average (-3.1%) for a quarter, but smaller than the 10-year average (-4.5%) and the 15-year average (-3.9%) for a quarter.

For more details, please see pages 2 and 3.

Guidance: Average % of S&P 500 Companies Issuing Negative EPS Guidance for Q4

The term “guidance” (or “preannouncement”) is defined as a projection or estimate for EPS provided by a company in advance of the company reporting actual results. Guidance is classified as negative if the estimate (or mid-point of a range estimates) provided by a company is lower than the mean EPS estimate the day before the guidance was issued. Guidance is classified as positive if the estimate (or mid-point of a range of estimates) provided by the company is higher than the mean EPS estimate the day before the guidance was issued.

At this point in time, 105 companies in the index have issued EPS guidance for Q4 2018. Of these 105 companies, 72 have issued negative EPS guidance and 33 have issued positive EPS guidance. The percentage of companies issuing negative EPS guidance is 69% (72 out of 105), which is slightly below the 5-year average of 70%.

Earnings Growth: 11.4%

The estimated (year-over-year) earnings growth rate for Q4 2018 is 11.4%. If 11.4% is the final growth rate for the quarter, it will mark the first time the index has not reported earnings growth above 20% since Q4 2017. However, it will mark the fifth straight quarter of double-digit earnings growth for the index. Ten of the eleven sectors are expected to report year-over-year growth in earnings. Six sectors are projected to report double-digit earnings growth, led by the Energy, Industrials, Financials, and Communication Services sectors.

Energy: Broad-Based Growth Expected

The Energy sector is expected to report the highest (year-over-year) earnings growth of all eleven sectors at 74.6%. At the sub-industry level, five of the six sub-industries in the sector are projected to report earnings growth for the quarter: Oil & Gas Drilling (N/A due to \$0 earnings in year-ago), Oil & Gas Exploration & Production (160%), Integrated Oil & Gas (73%), Oil & Gas Storage & Transportation (69%), and Oil & Gas Refining & Marketing (56%). The Oil & Gas Equipment & Services (-8%) sub-industry is the only sub-industry expected to report a year-over-year decline in earnings in the sector.

Industrials: 8 of 12 Industries Expected to Report Double-Digit Growth

The Industrials sector is expected to report the second highest (year-over-year) earnings growth of all eleven sectors at 14.5%. At the industry level, 9 of the 12 industries in this sector are predicted to report earnings growth for the quarter. Eight of these nine industries are projected to report double-digit growth in earnings, led by the Construction & Engineering (54%), Trading Companies & Distributors (39%), and Road & Rail (31%) industries. At the company level, General Electric is the largest detractor to earnings growth for the sector. The mean EPS estimate for GE for Q4 2018 is \$0.22, compared to actual EPS of \$0.27 in the year-ago quarter. If this company were excluded, the estimated earnings growth rate for the sector would improve to 17.3% from 14.5%.

Financials: 4 of 5 Industries Expected to Report Double-Digit Growth

The Financials sector is expected to report the third highest (year-over-year) earnings growth of all eleven sectors at 13.6%. At the industry level, four of the five industries in this sector are predicted to report earnings growth for the quarter. All Four of these industries are projected to report double-digit growth in earnings: Diversified Financial Services (58%), Consumer Finance (27%), Banks (16%), and Capital Markets (12%). The Insurance (-1%) industry is the only industry expected to report a year-over-year decline in earnings for the quarter.

Communication Services: 2 of 4 Industries Expected to Report Double-Digit Growth

The Communication Services sector is expected to report the fourth highest (year-over-year) earnings growth of all eleven sectors at 13.3%. At the industry level, three of the four industries in this sector are predicted to report earnings growth for the quarter. Two of these three industries are projected to report double-digit growth in earnings: Diversified Telecommunications Services (30%) and Media (24%).

Revenue Growth: 6.1%

The estimated (year-over-year) revenue growth rate for Q4 2018 is 6.1%. Ten of the eleven sectors are expected to report year-over-year growth in revenues. Four sectors are projected to report double-digit growth in revenues: Communication Services, Energy, Real Estate, and Materials.

Communication Services: Alphabet Leads Growth

The Communication Services sector is expected to report the highest (year-over-year) revenue growth of all eleven sectors at 20.1%. At the industry level, all four industries in this sector are predicted to report revenue growth. Two of these four industries are projected to report double-digit revenue growth: Interactive Media & Services (45%) and Media (17%). At the company level, Alphabet is projected to be the largest contributor to revenue growth for this sector. The mean revenue estimate for Alphabet for Q4 2018 is \$38.9 billion, compared to revenue of \$25.9 billion in the year-ago quarter. Because Alphabet is a dual-listed ticker in the index, the company's revenue numbers are counted twice in the growth rate calculation (once for GOOG and once for GOOGL). If this company were excluded, the estimated revenue growth rate for this sector would fall to 12.0% from 20.1%.

Energy: 4 of 6 Sub-Industries Expected to Report Double-Digit Growth

The Energy sector is expected to report the second highest (year-over-year) revenue growth of all eleven sectors at 11.3%. At the sub-industry level, five of the six sub-industries are predicted to report revenue growth. Four of these five sub-industries are projected to report double-digit revenue growth: Oil & Gas Drilling (27%), Oil & Gas Refining & Marketing (16%), Oil & Gas Exploration & Production (14%), and Integrated Oil & Gas (10%).

Real Estate: CBRE Group Leads Growth

The Real Estate sector is expected to report the third highest (year-over-year) revenue growth of all eleven sectors at 10.9%. At the company level, CBRE Group is projected to be the largest contributor to revenue growth for the sector. The mean revenue estimate for CBRE Group for Q4 2018 is \$5.95 billion, compared to revenue of \$4.34 billion in the year-ago quarter. If this company were excluded, the revenue growth rate for the sector would fall to 5.3% from 10.9%.

Materials: Linde Leads Growth on Easy Comparison to Standalone Revenue for Praxair

The Materials sector is expected to report the fourth highest (year-over-year) revenue growth of all eleven sectors at 10.2%. At the industry level, three of the four industries in this sector are predicted to report revenue growth, led by the Chemicals (14%) industry. At the company level, Linde plc is projected to be the largest contributor to revenue growth for the sector. However, the estimated revenues for Q4 2018 (\$7.25 billion) reflect the combination of Praxair and Linde, while the actual revenues for Q4 2017 (\$2.95 billion) reflect the standalone Praxair company. This apple-to-orange comparison is the main reason Linde plc is expected to be the largest contributor to revenue growth for the sector. If this company were excluded, the estimated revenue growth rate for the sector would fall to 5.4% from 10.2%.

Looking Ahead: Forward Estimates and Valuation

Single-Digit Growth Projected for First 3 Quarters of 2019

For the fourth quarter, analysts expect companies to report earnings growth of 11.4% and revenue growth of 6.1%. For CY 2018, analysts are projecting companies to report earnings growth of 20.2% and revenue growth of 8.8%. However, analysts expect single-digit earnings growth for the first three quarters of 2019.

For Q1 2019, analysts are projecting earnings growth of 2.9% and revenue growth of 7.3%.

For Q2 2019, analysts are projecting earnings growth of 3.7% and revenue growth of 6.0%.

For Q3 2019, analysts are projecting earnings growth of 4.3% and revenue growth of 5.8%.

For Q4 2019, analysts are projecting earnings growth of 12.1% and revenue growth of 6.9%.

For CY 2019, analysts are projecting earnings growth of 7.4% and revenue growth of 6.0%.

Valuation: Forward P/E Ratio is 14.1, Below the 10-Year Average (14.6)

The forward 12-month P/E ratio is 14.1. This P/E ratio is below the 5-year average of 16.4 and below the 10-year average of 14.6. It is also below the forward 12-month P/E ratio of 16.8 recorded at the start of the fourth quarter (September 30). Since the start of the fourth quarter (September 30), the price of the index has decreased by 16.0%, while the forward 12-month EPS estimate has decreased by 0.1%.

Prior to the past few weeks, the last time the forward 12-month P/E ratio for the S&P 500 was 14.1 or lower was October 15, 2013 (14.0).

At the sector level, the Consumer Discretionary (18.0) sector has the highest forward 12-month P/E ratio, while the Financials (10.3) sector has the lowest forward 12-month P/E ratio.

Targets & Ratings: Analysts Project 26% Increase in Price Over Next 12 Months

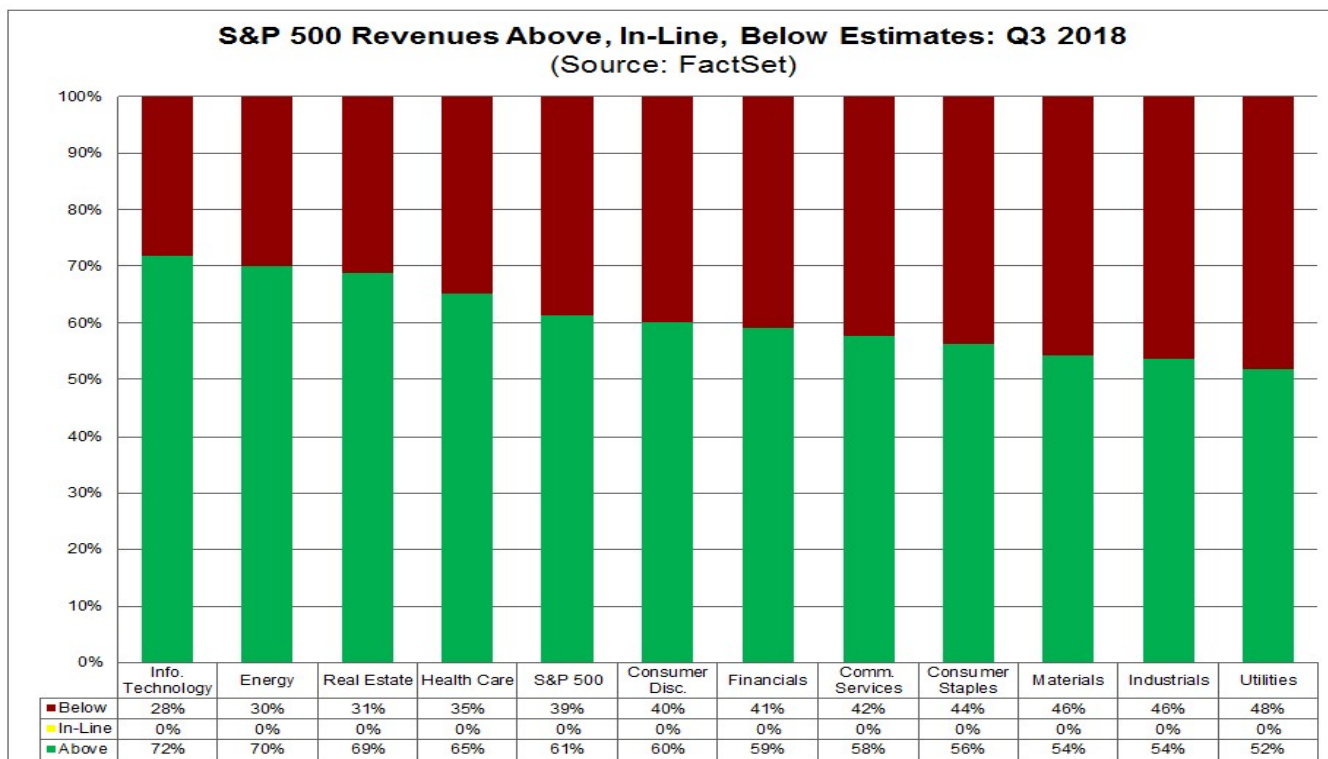
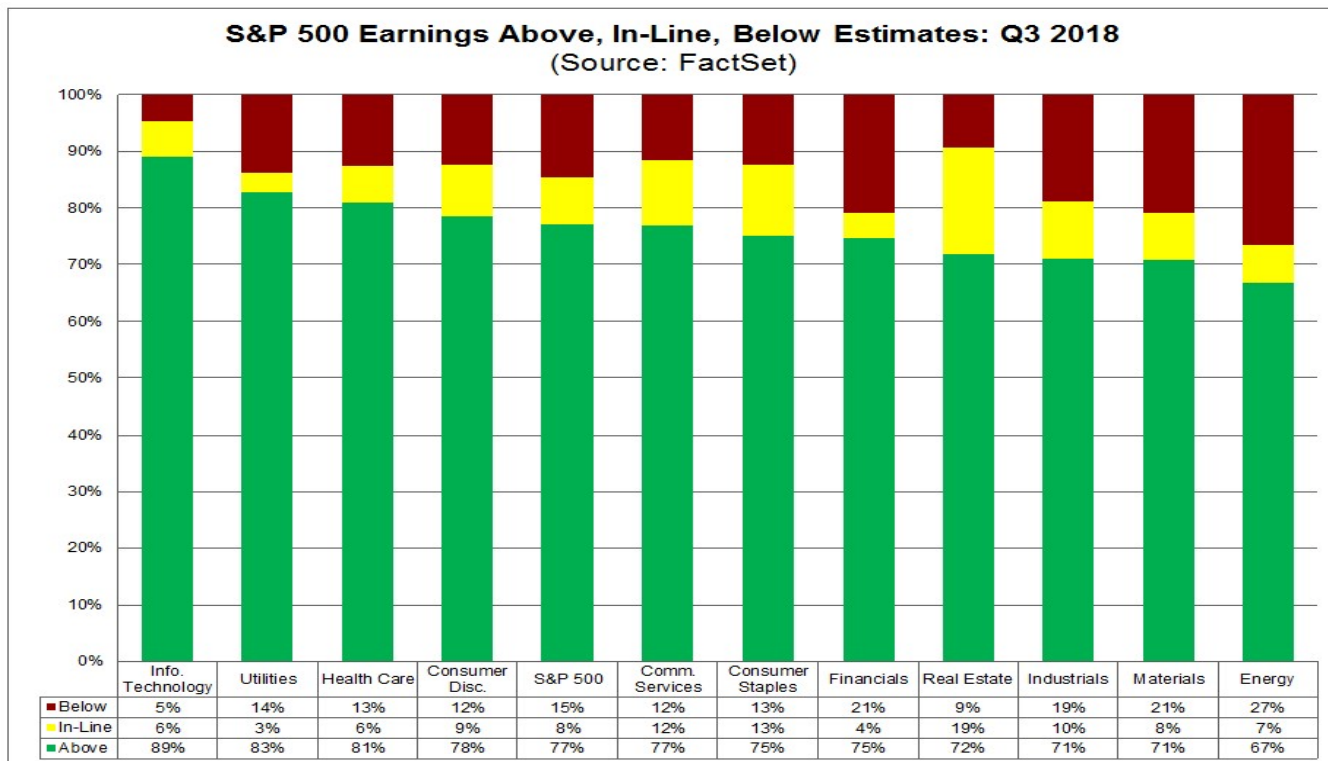
The bottom-up target price for the S&P 500 is 3093.95, which is 26.4% above the closing price of 2447.89. At the sector level, the Energy (+37.6%) sector is expected to see the largest price increase, as this sector has the largest upside difference between the bottom-up target price and the closing price. On the other hand, the Utilities (+9.3%) sector is expected to see the smallest price increase, as this sector has the smallest upside difference between the bottom-up target price and the closing price.

Overall, there are 11,116 ratings on stocks in the S&P 500. Of these 11,116 ratings, 54.9% are Buy ratings, 40.0% are Hold ratings, and 5.1% are Sell ratings. At the sector level, the Energy (67%) sector has the highest percentage of Buy ratings, while the Consumer Staples (41%) sector has the lowest percentage of Buy ratings.

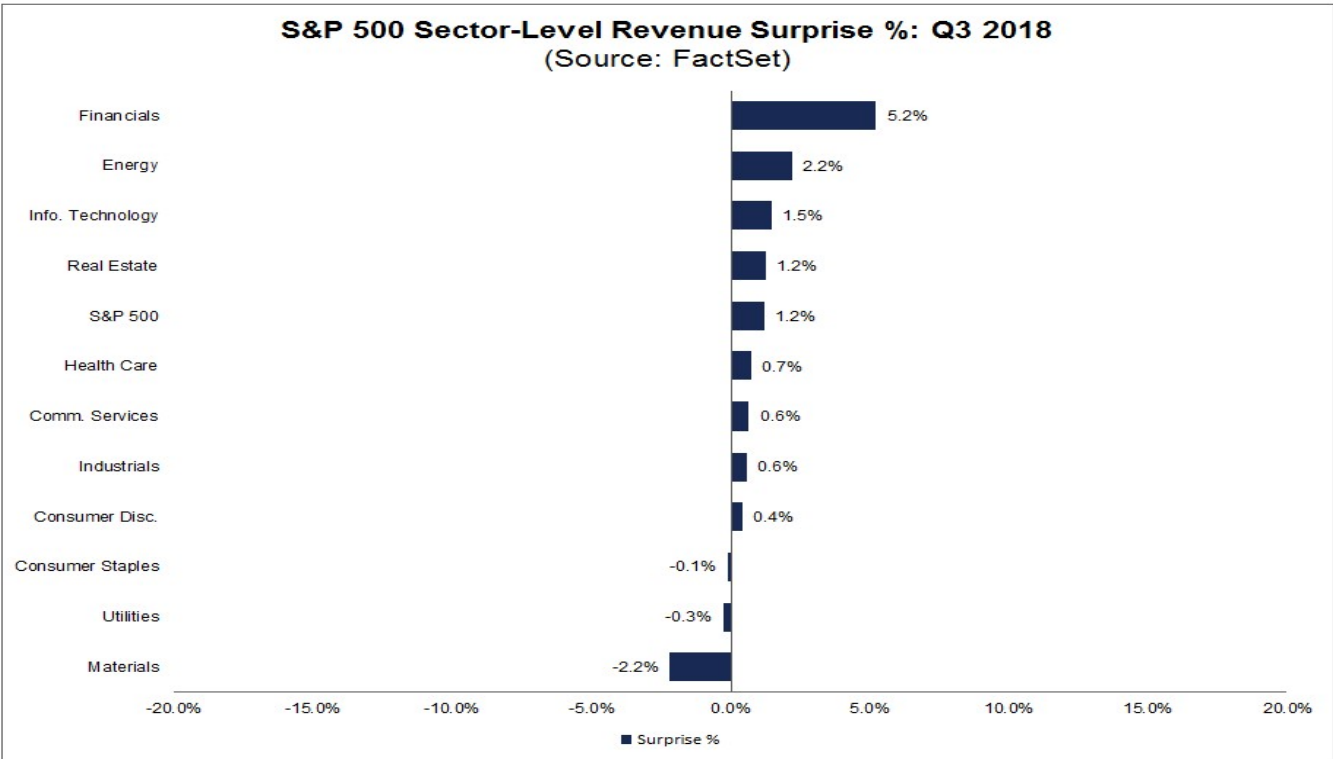
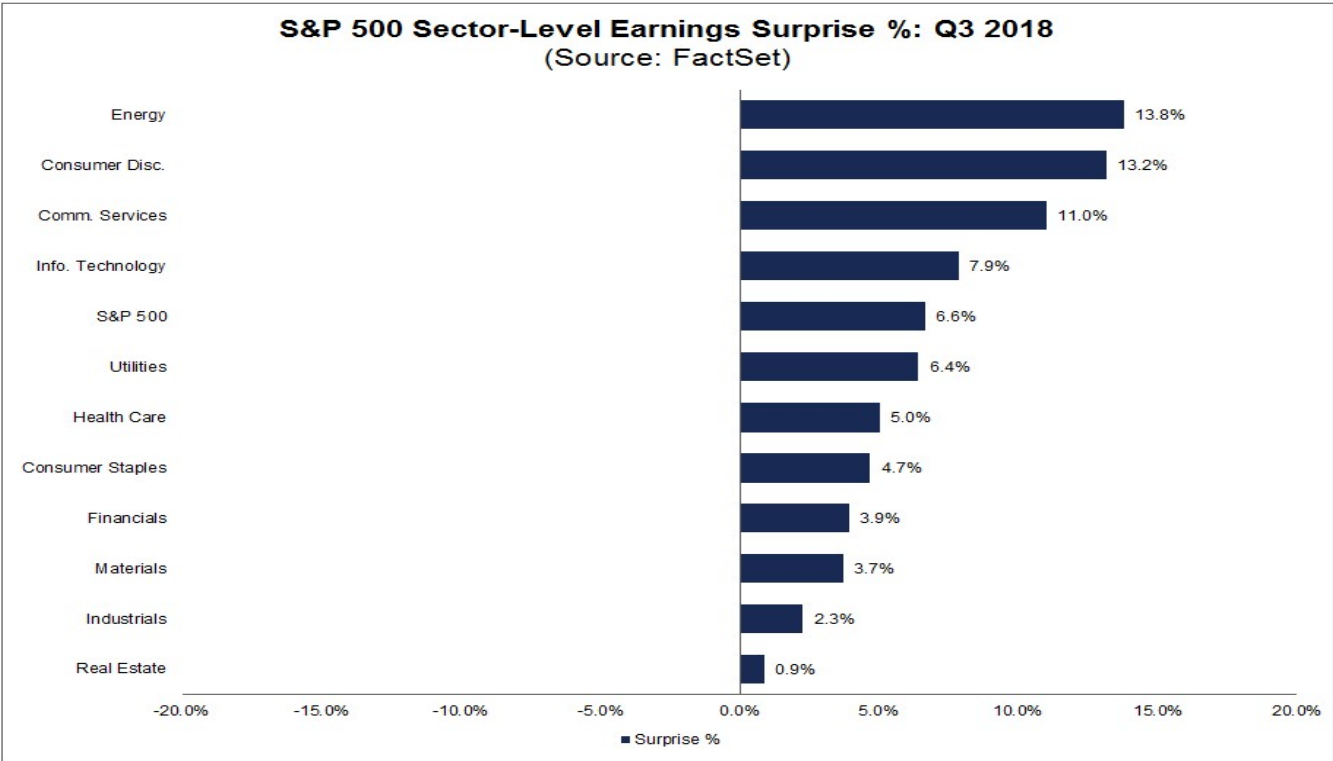
Companies Reporting Next Week: 2

During the upcoming week, two S&P 500 companies are scheduled to report results for the fourth quarter.

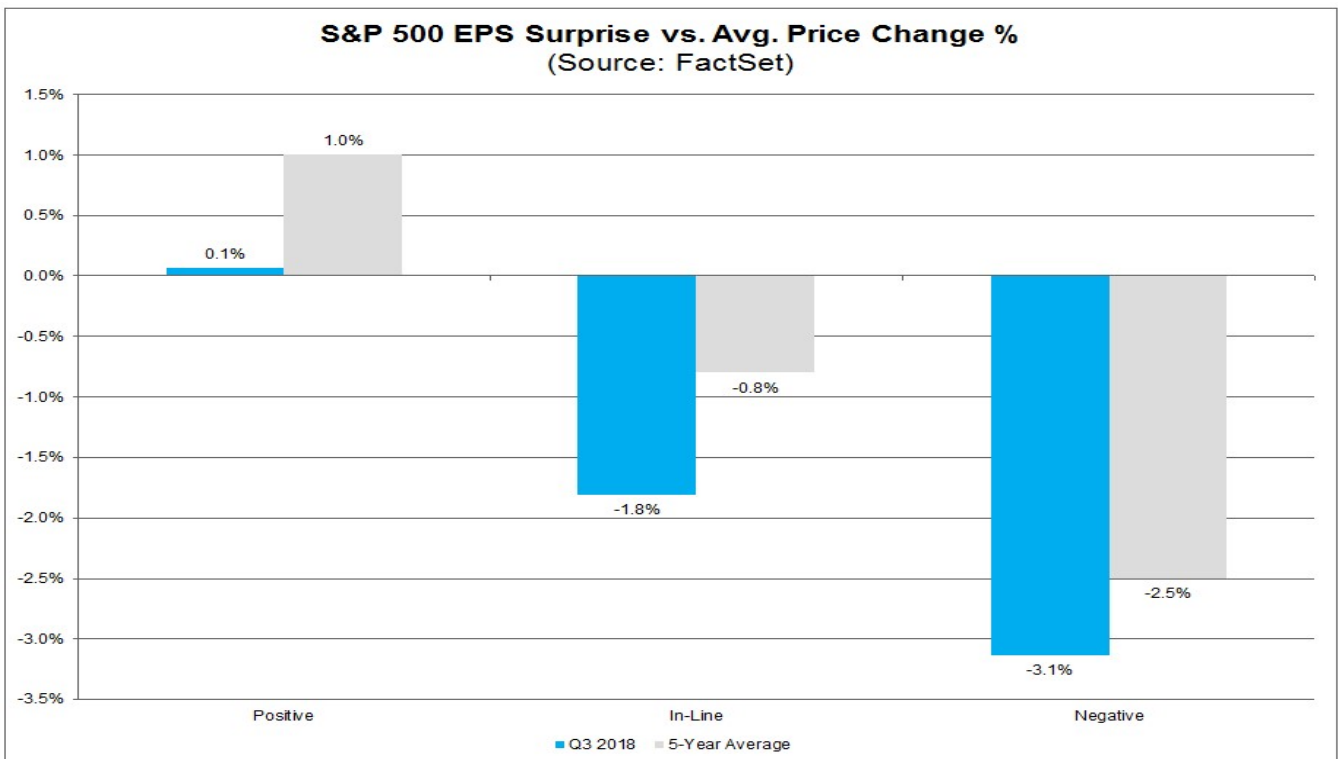
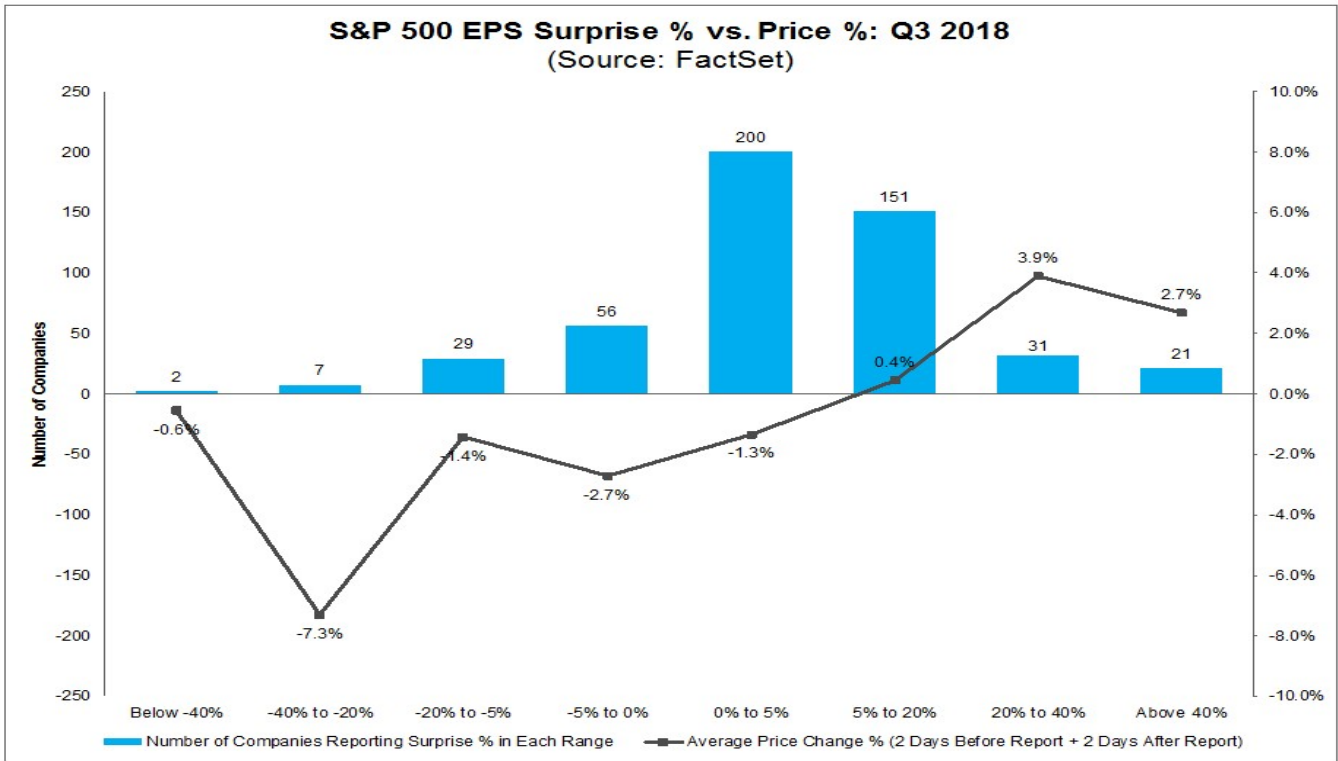
Q3 2018: Scorecard



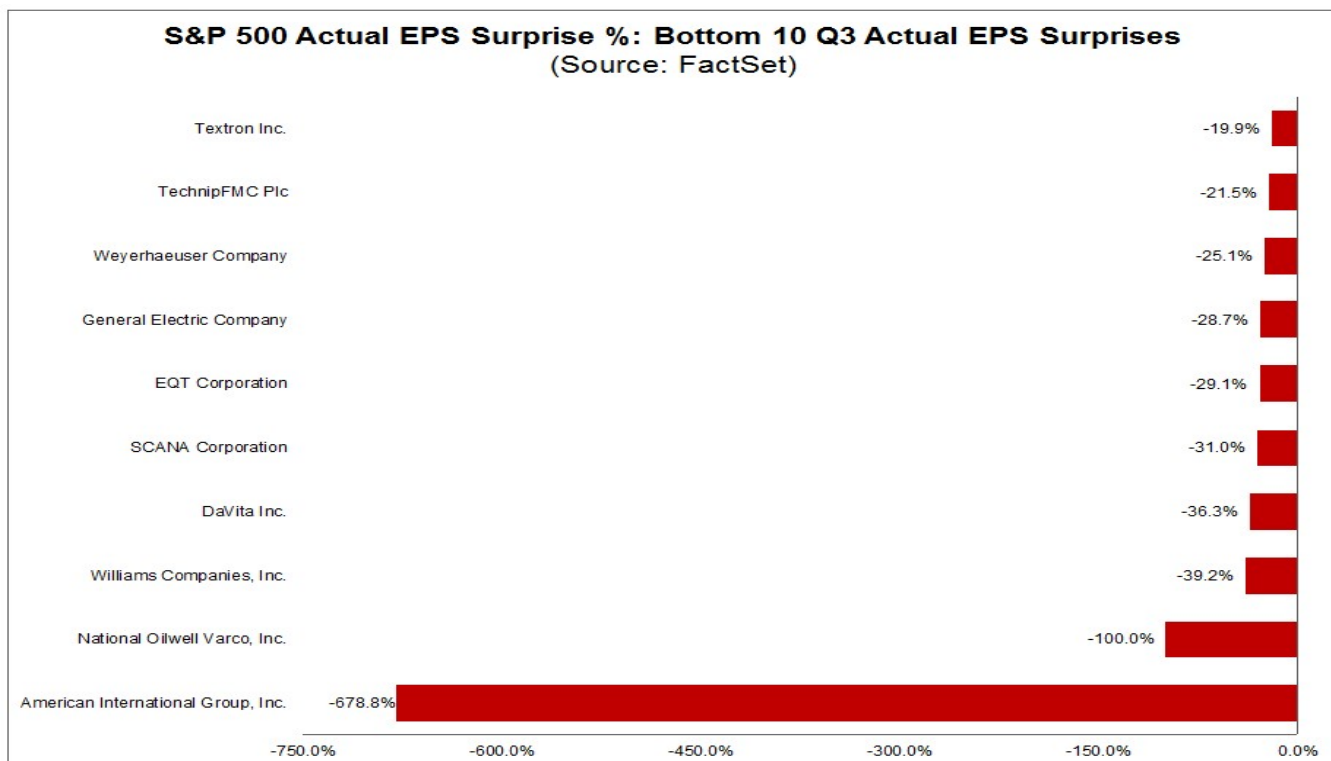
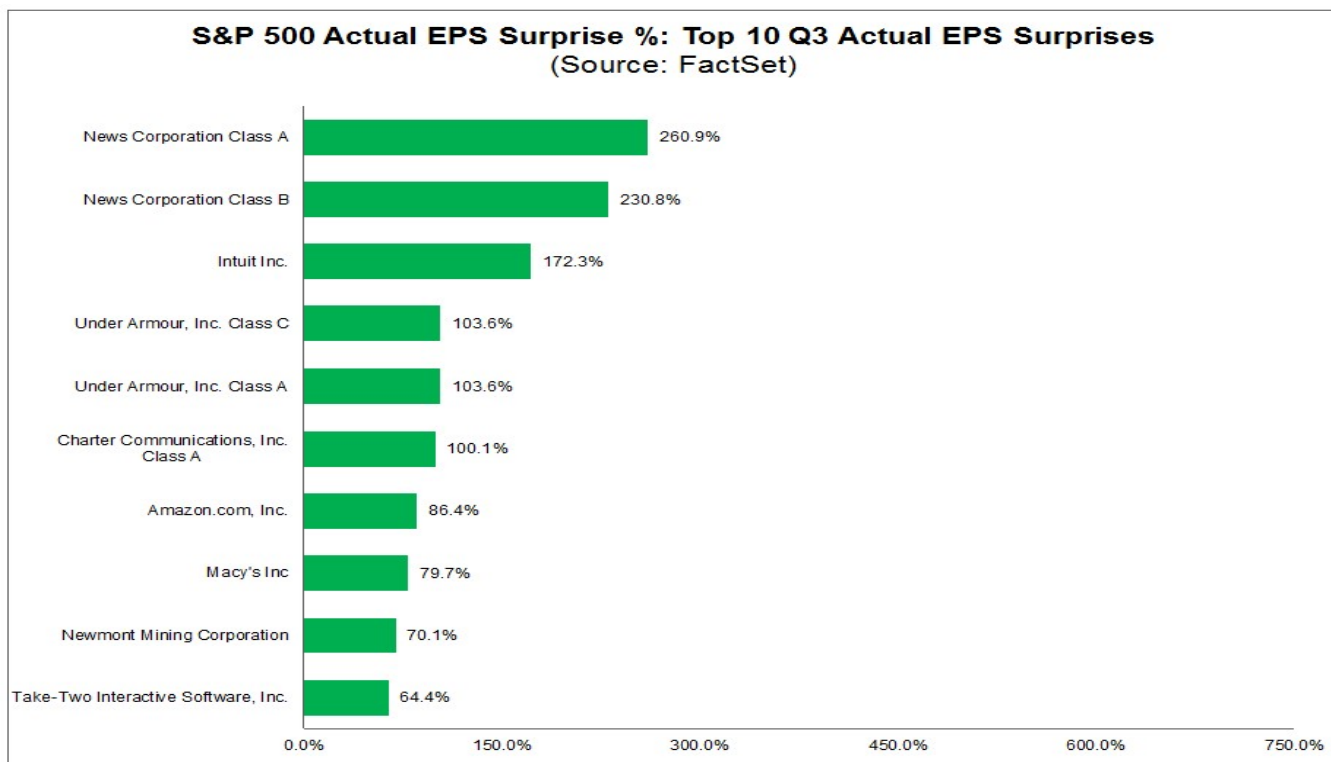
Q3 2018: Scorecard



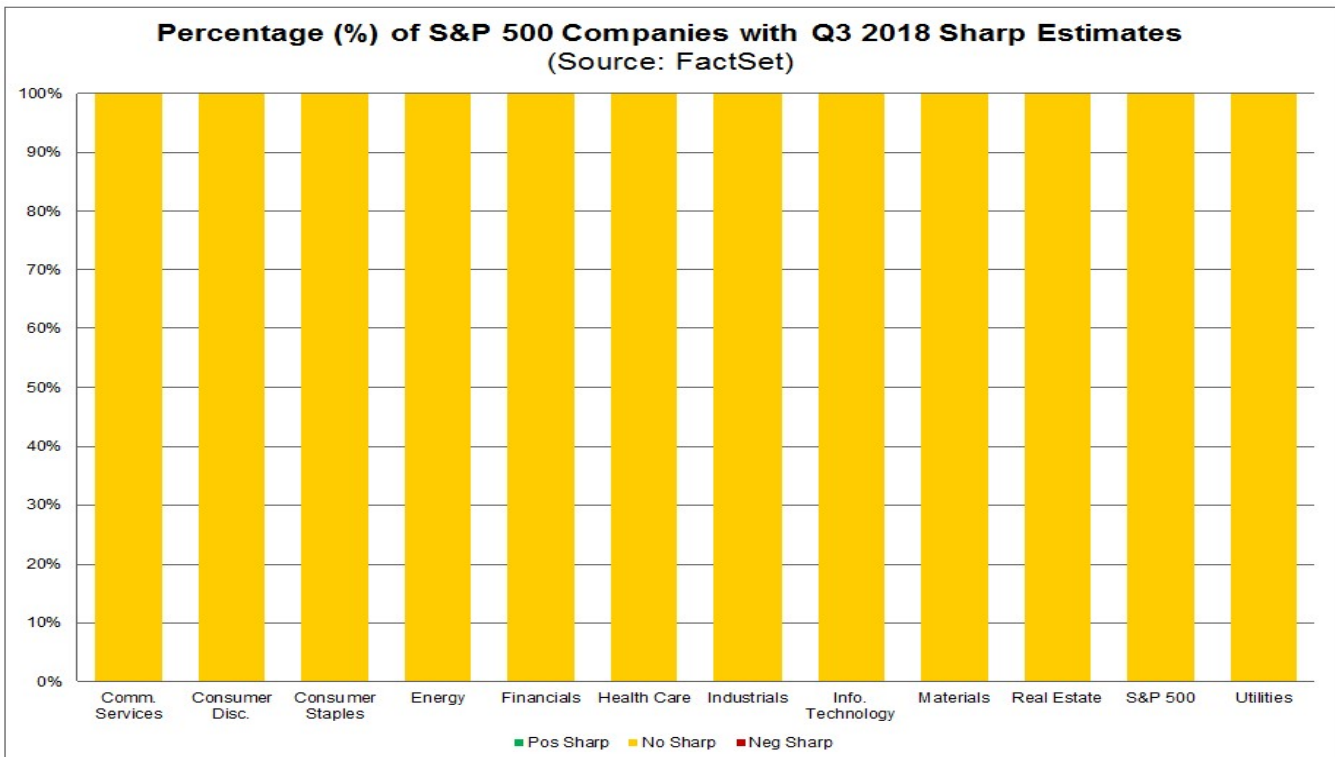
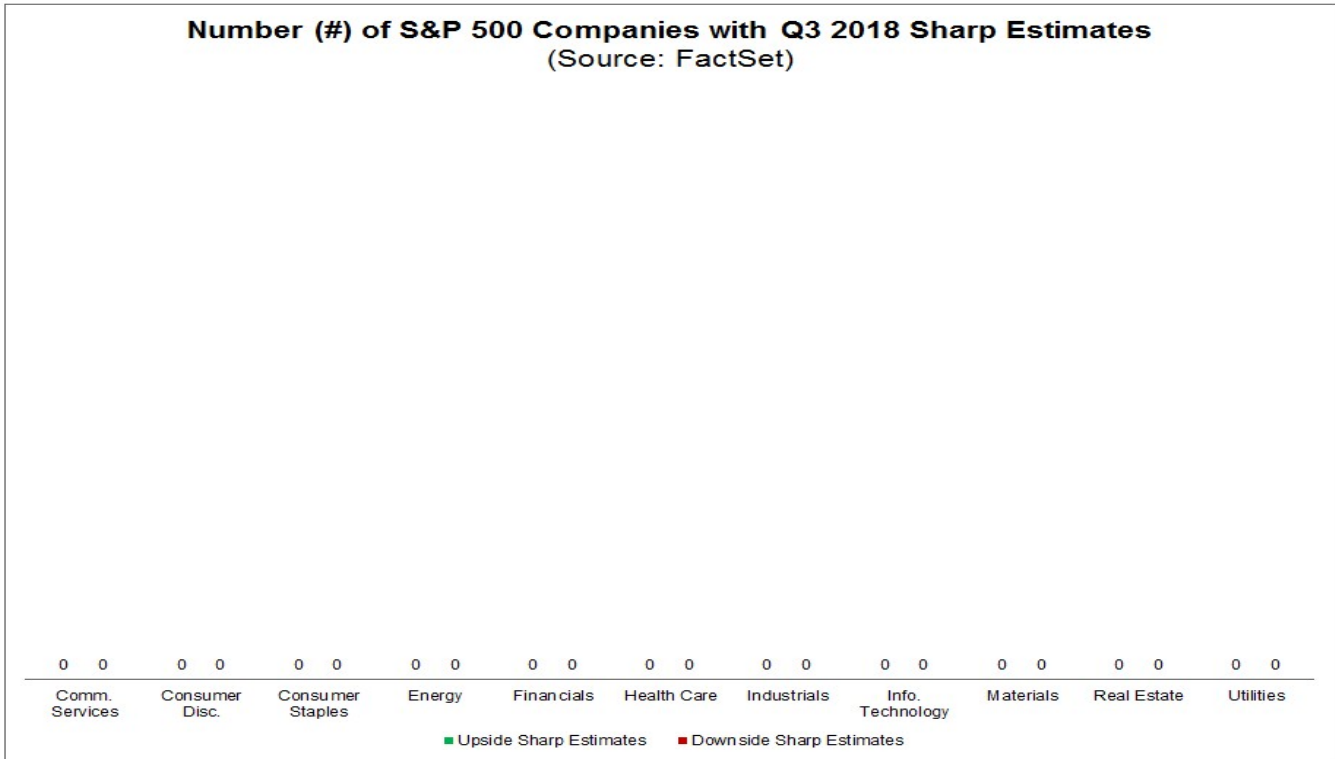
Q3 2018: Scorecard



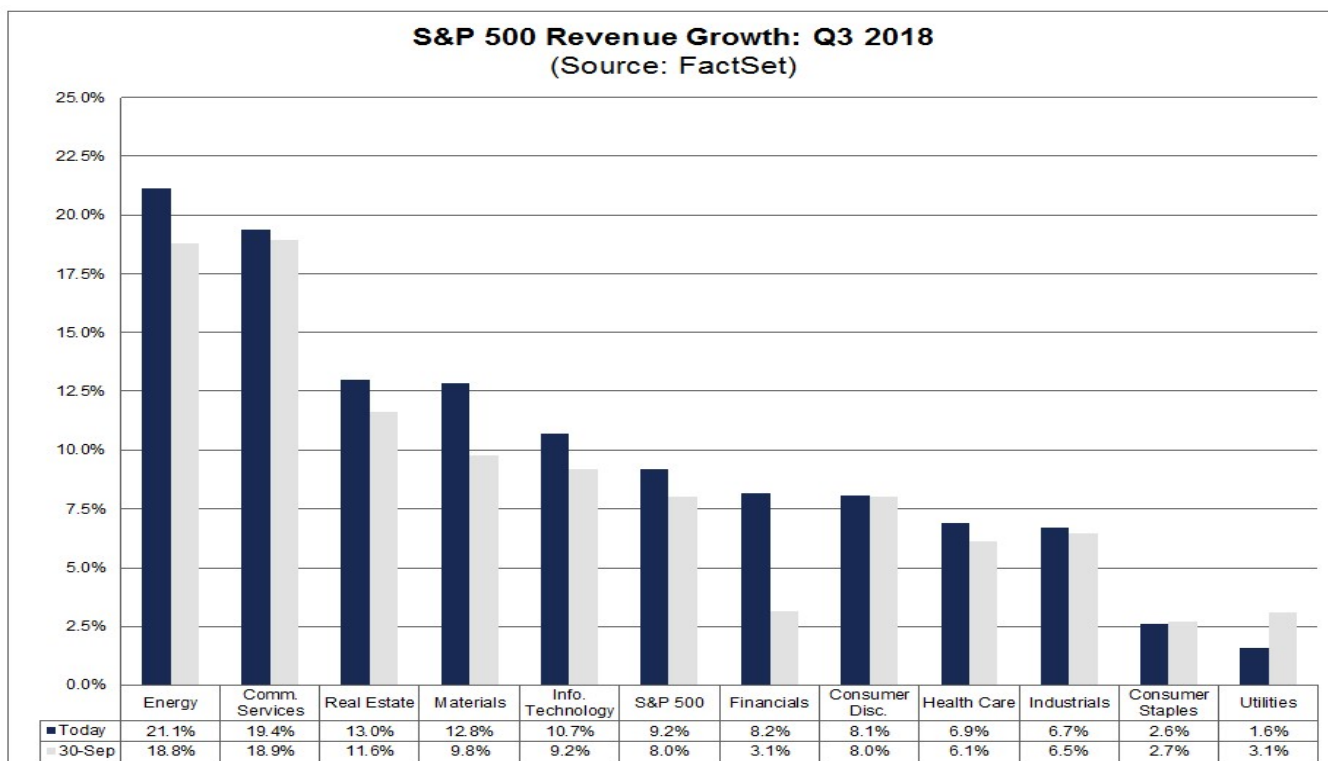
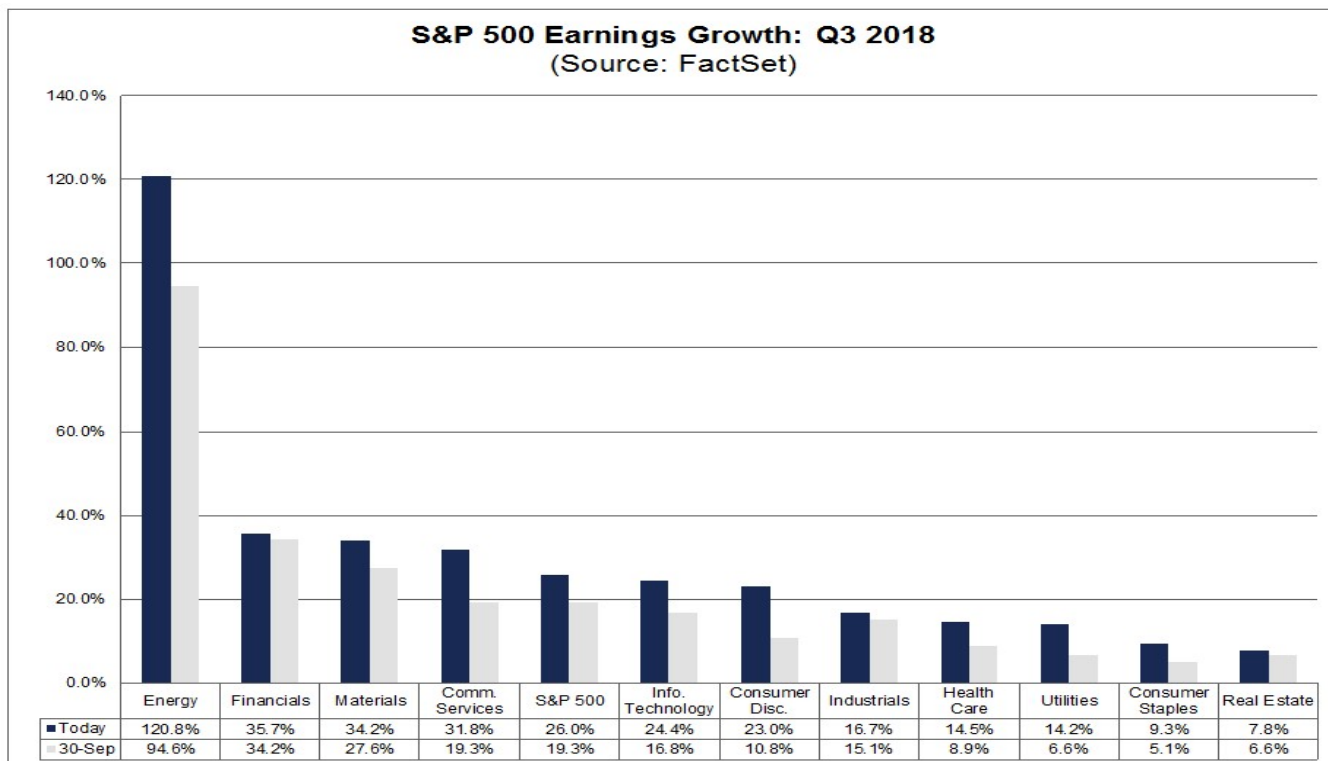
Q3 2018: Scorecard



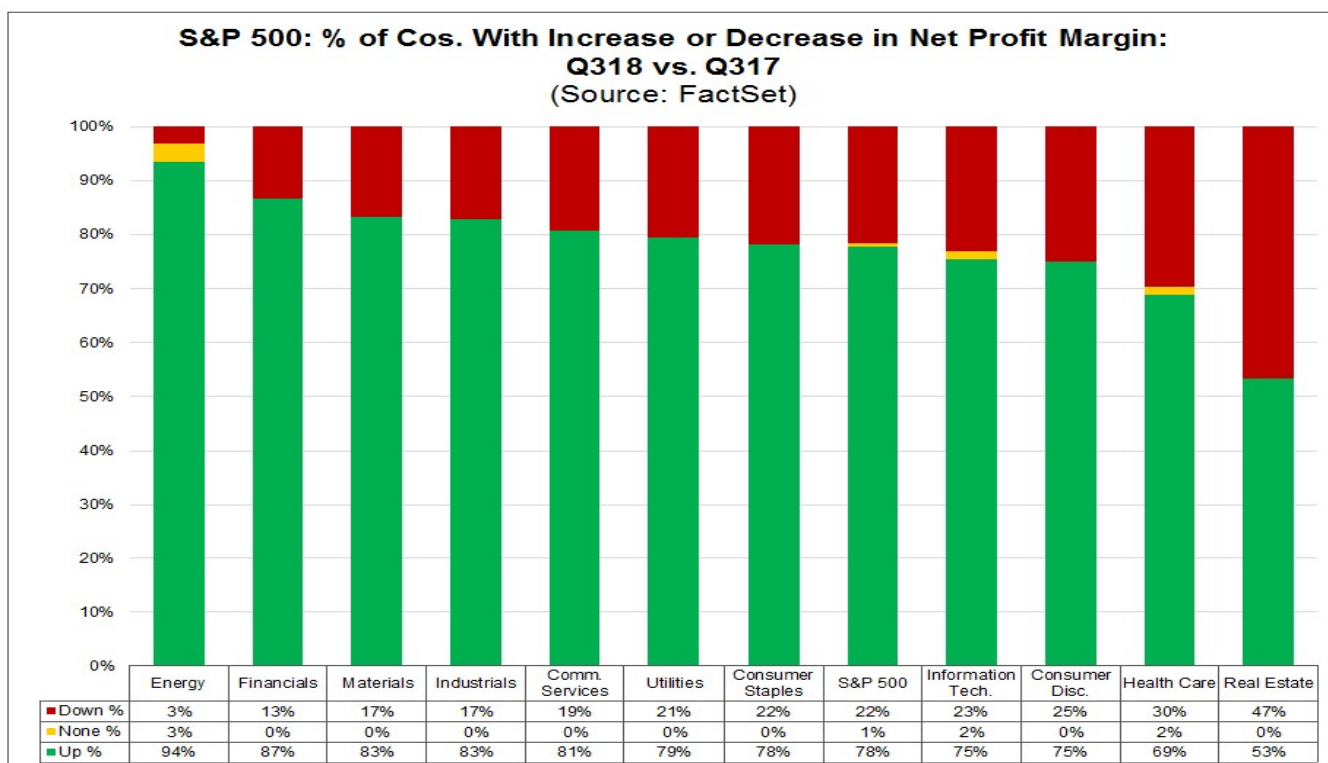
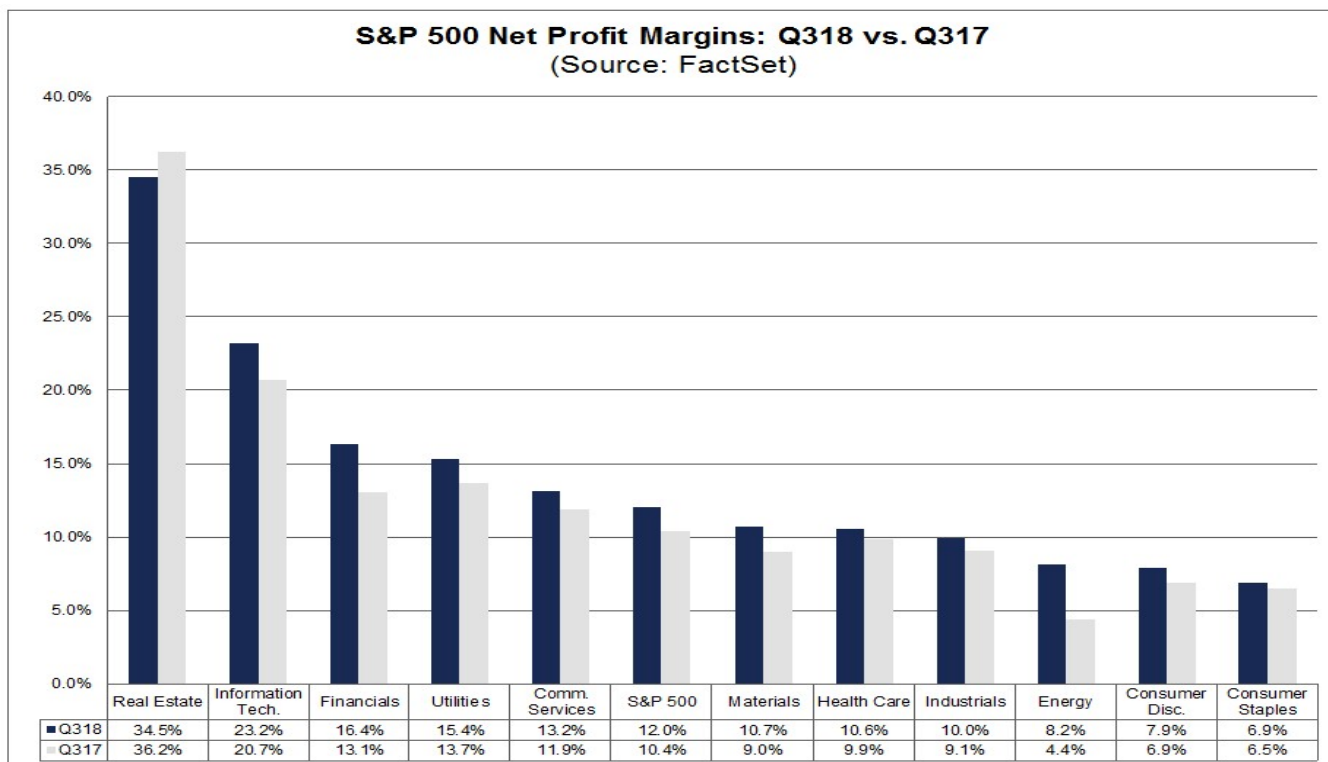
Q3 2018: Projected EPS Surprises (Sharp Estimates)



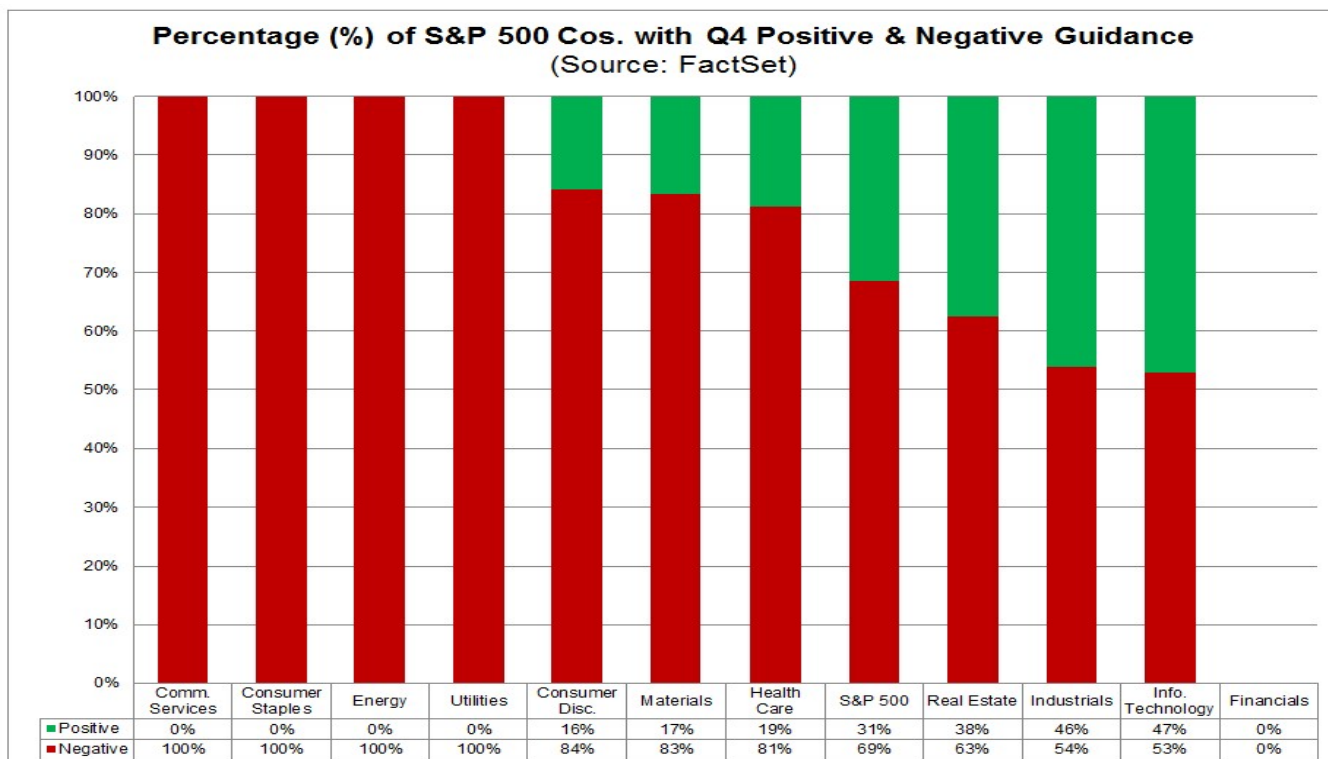
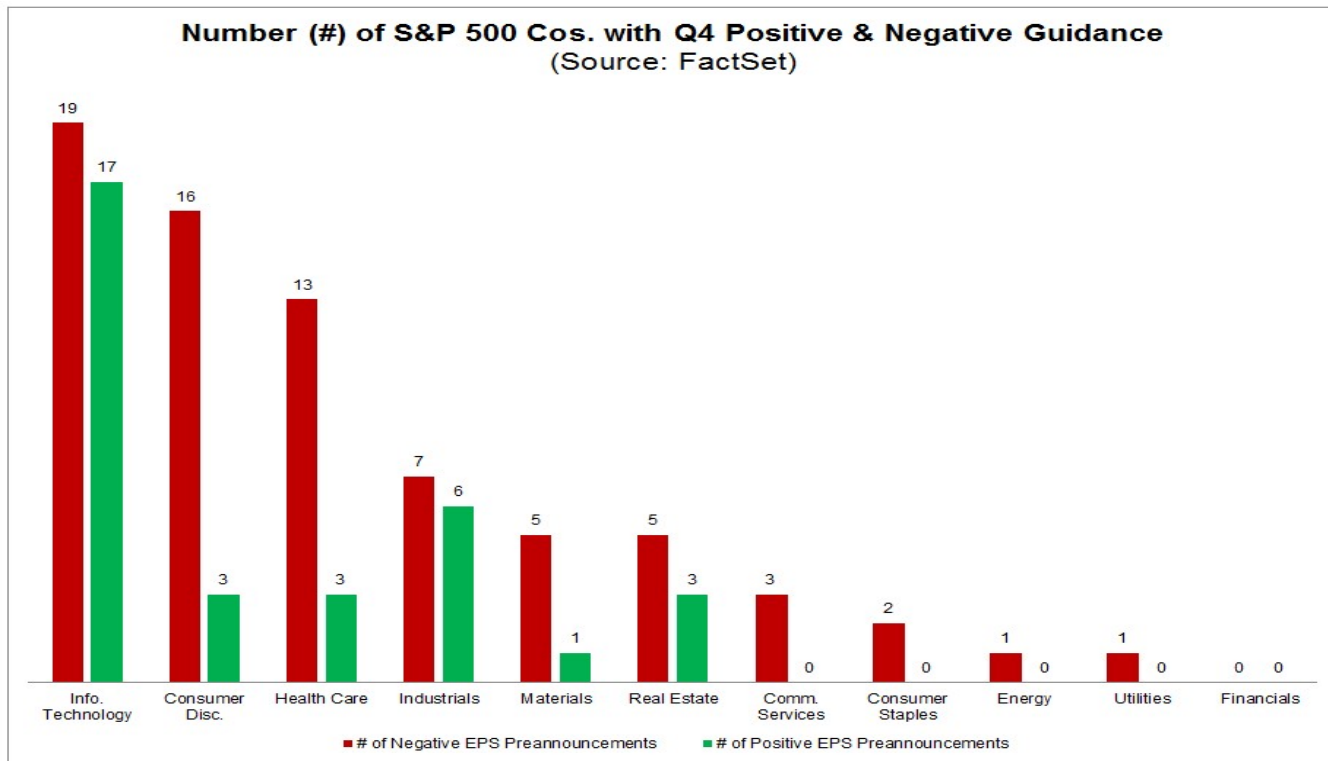
Q3 2018: Growth



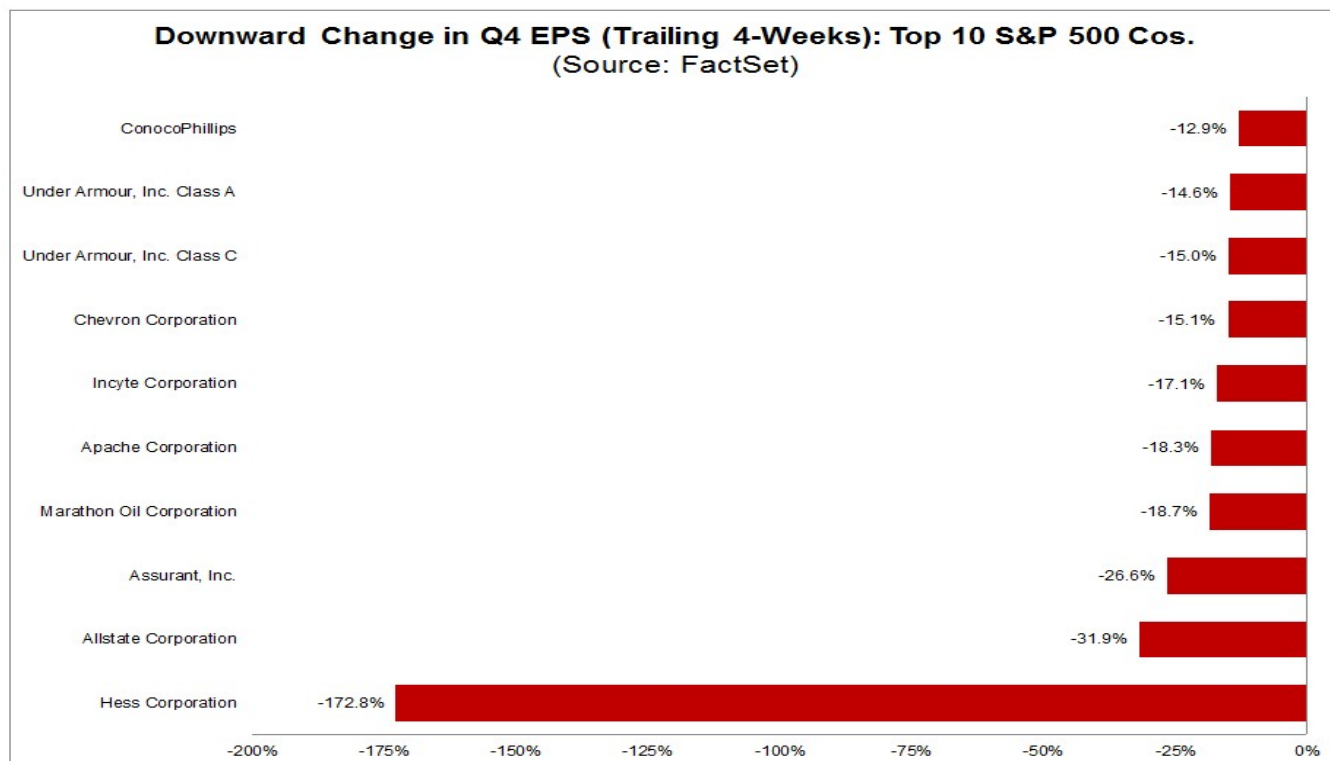
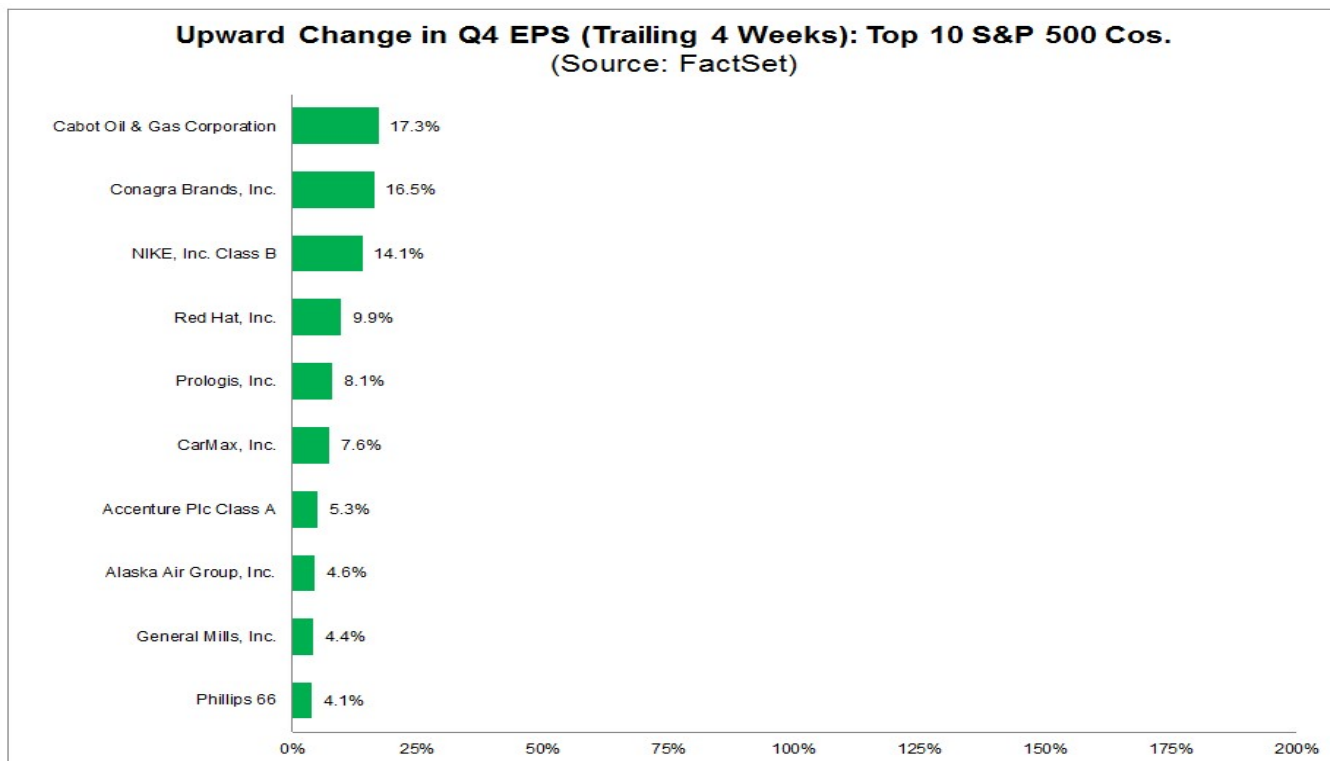
Q3 2018: Net Profit Margin



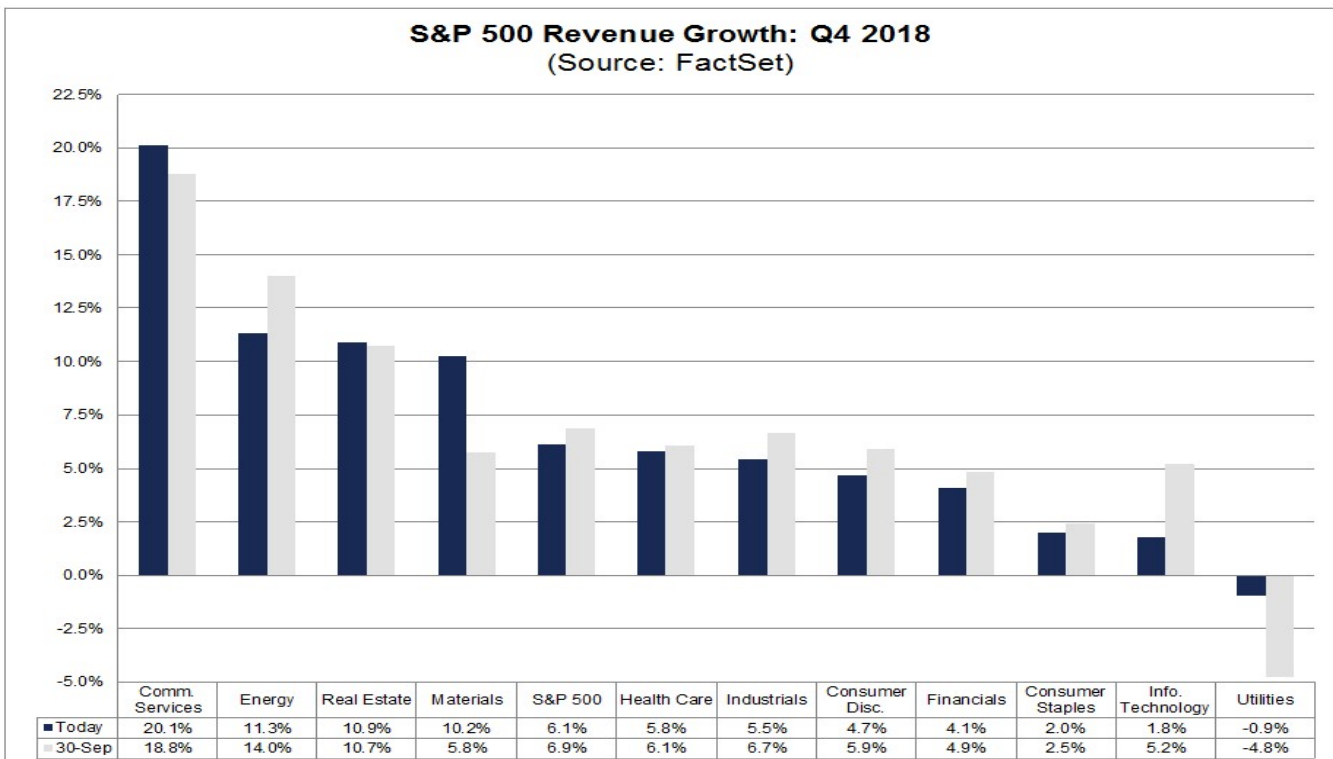
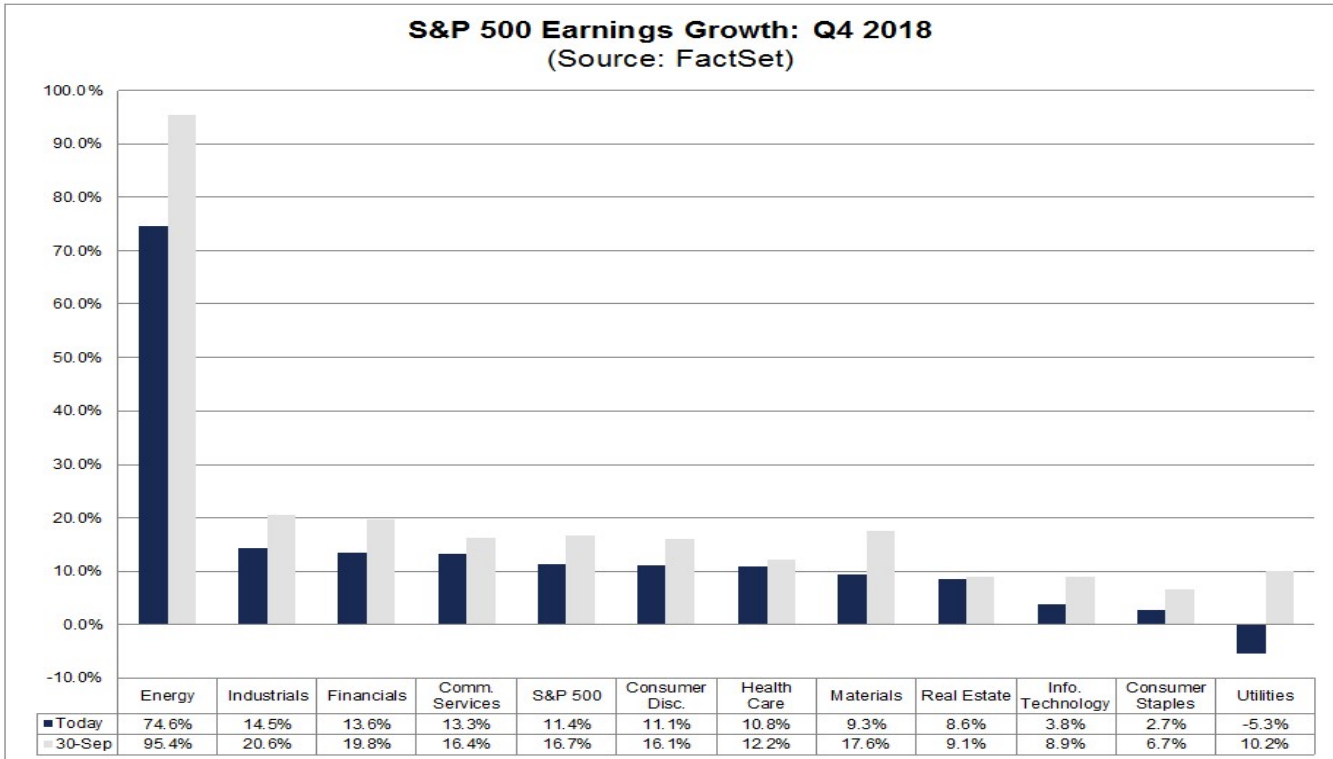
Q4 2018: EPS Guidance



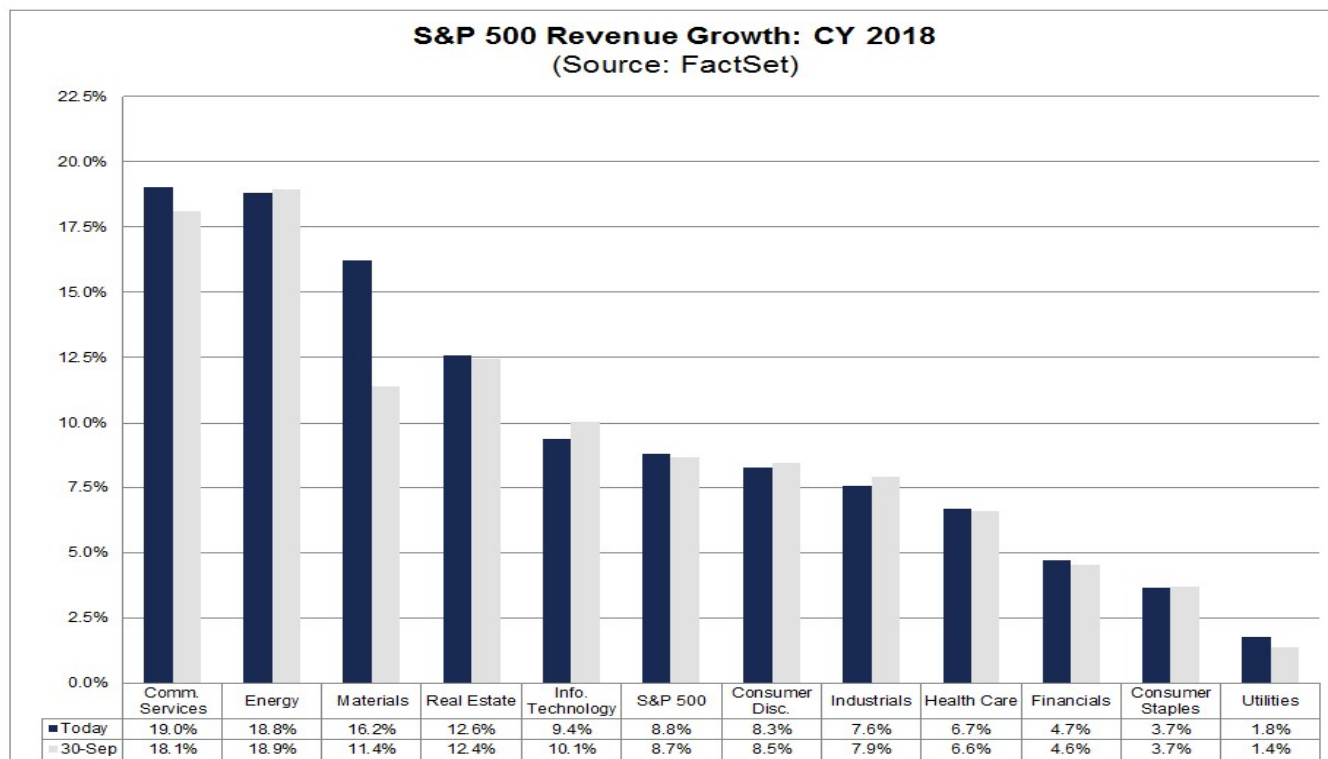
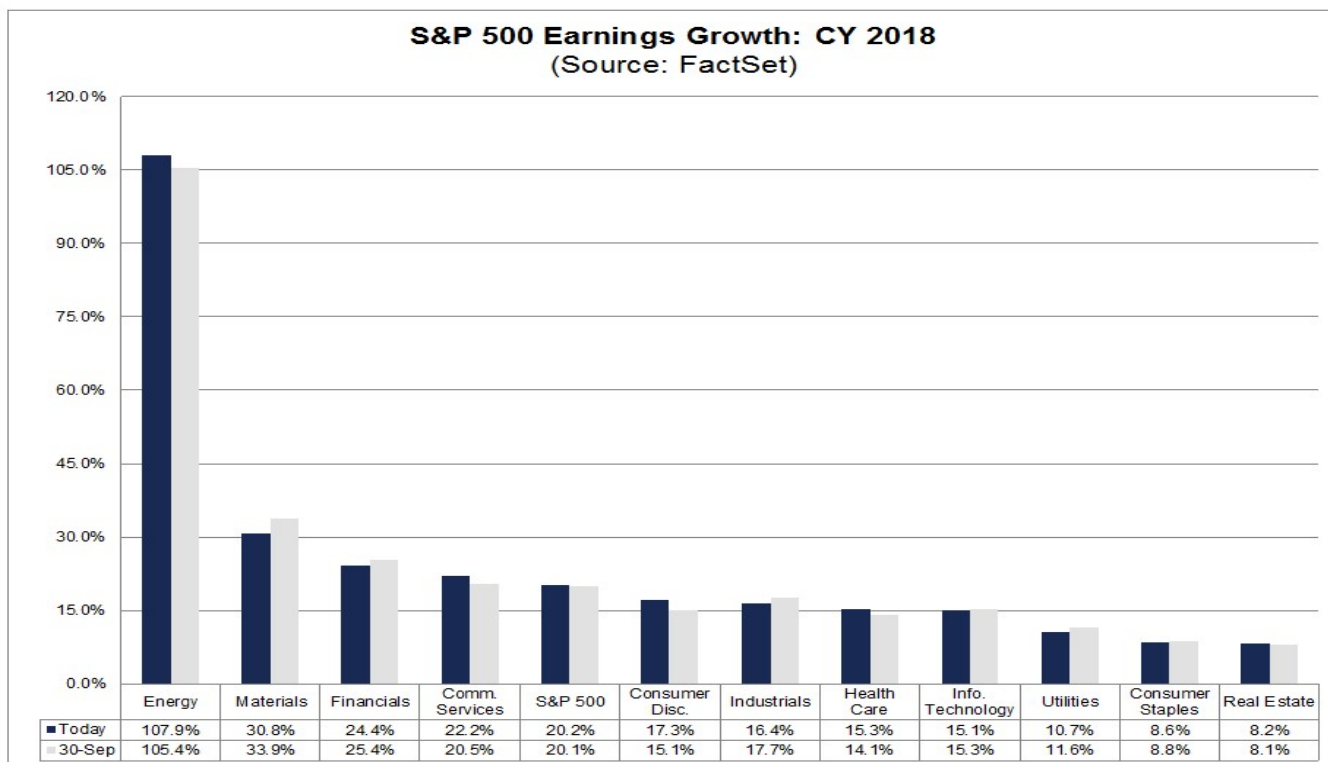
Q4 2018: EPS Revisions



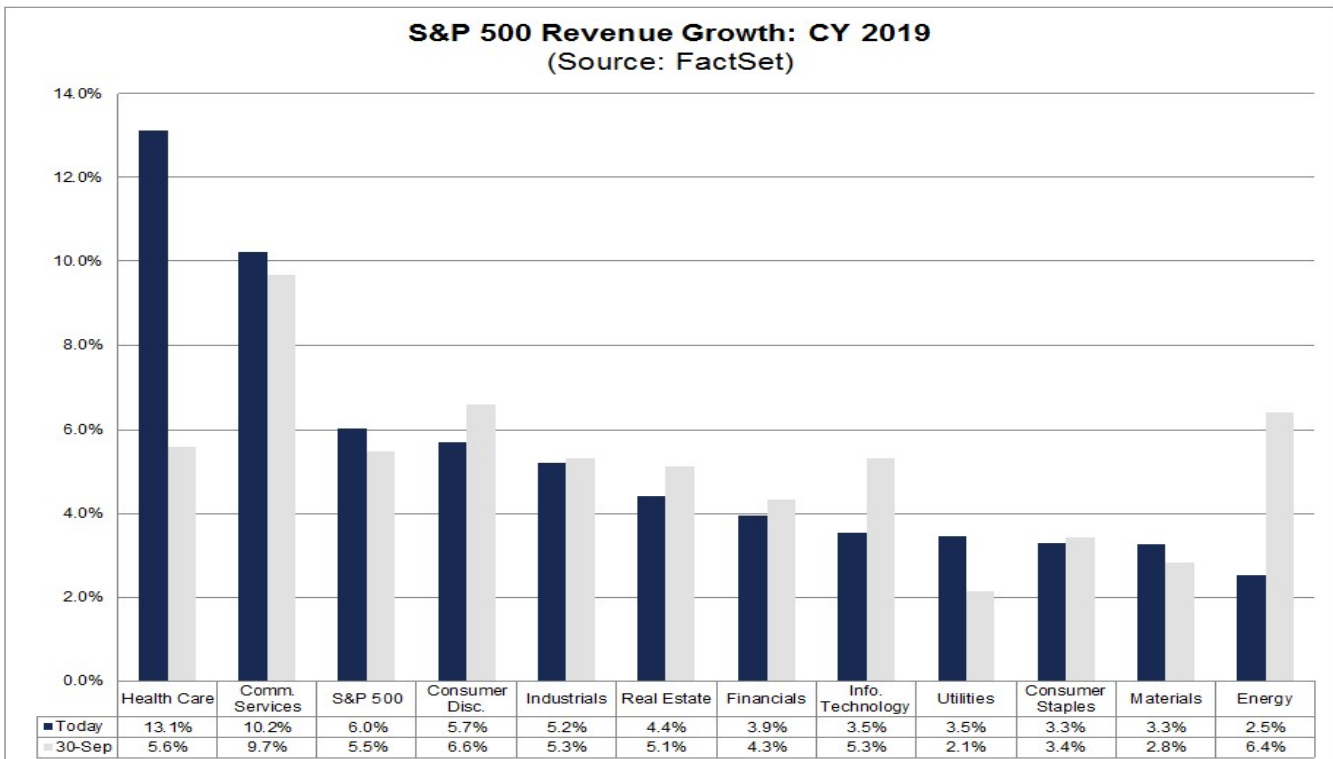
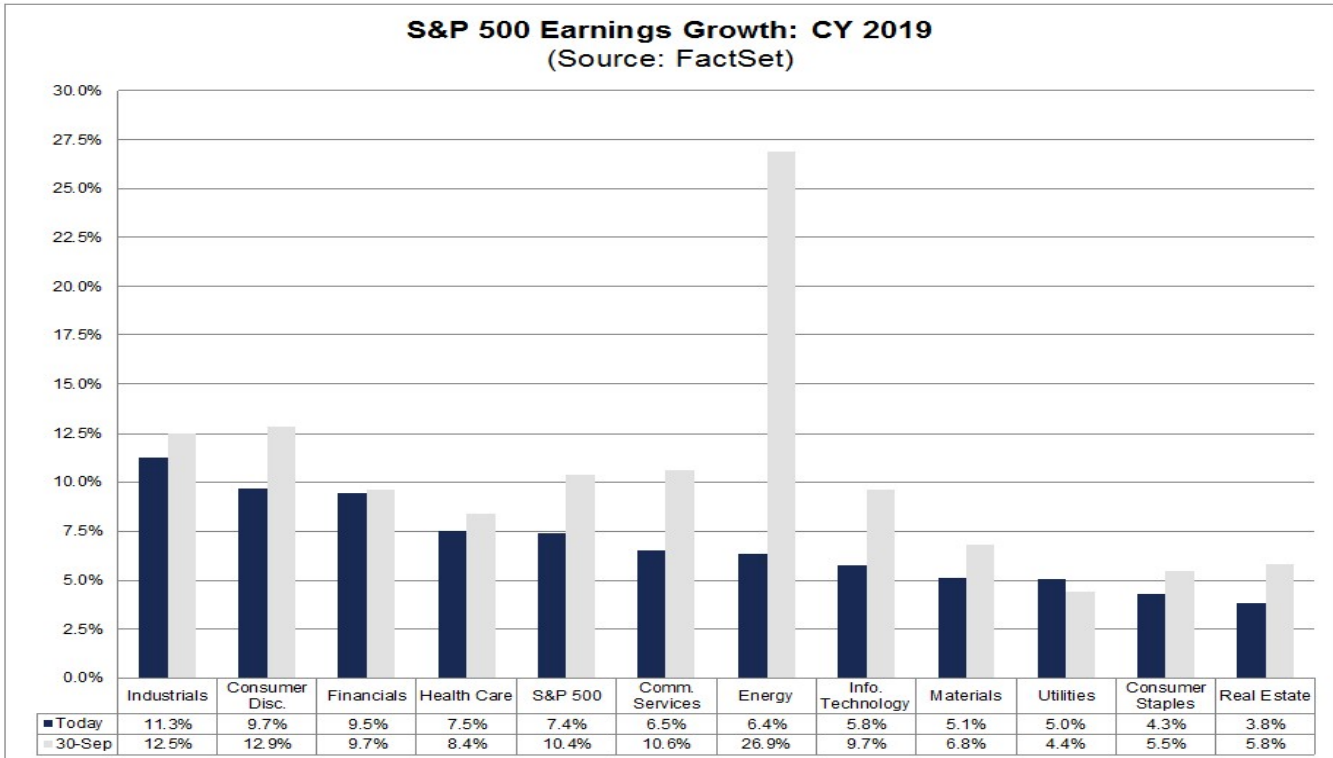
Q4 2018: Growth



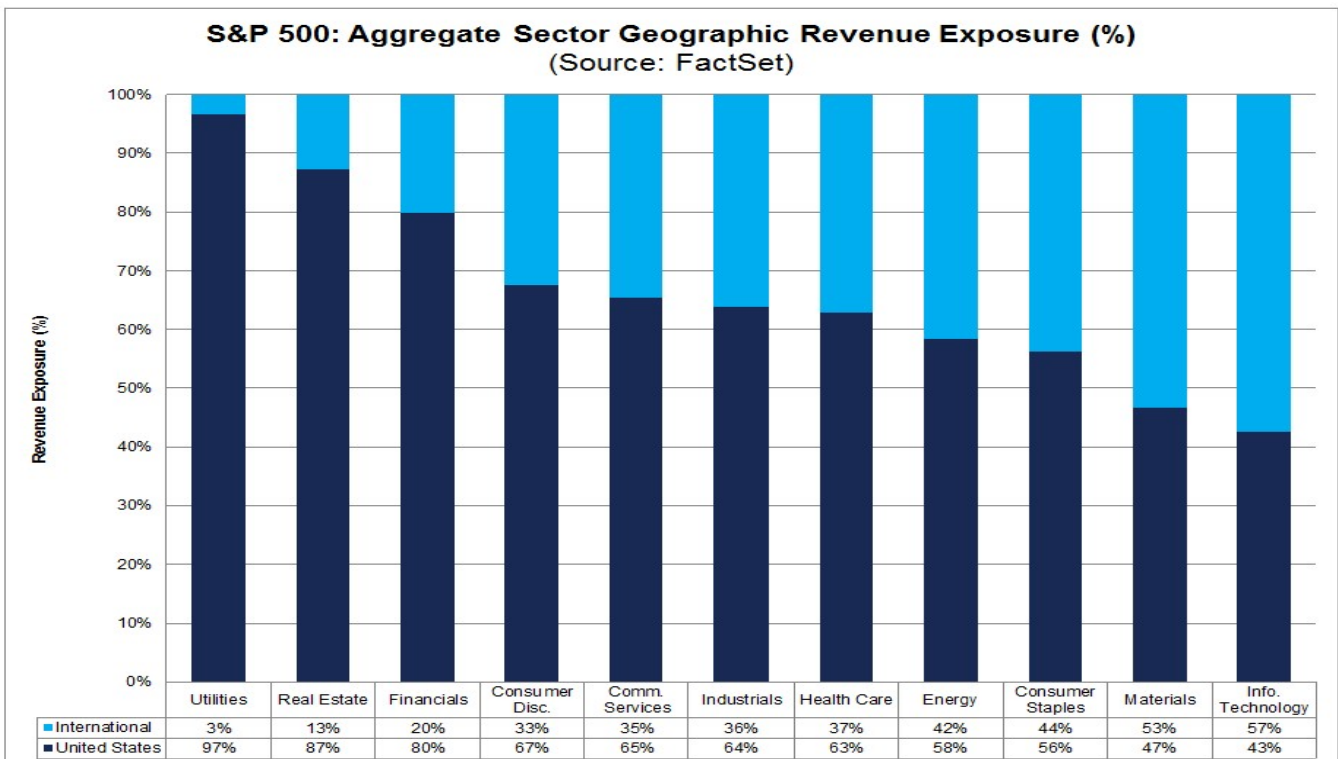
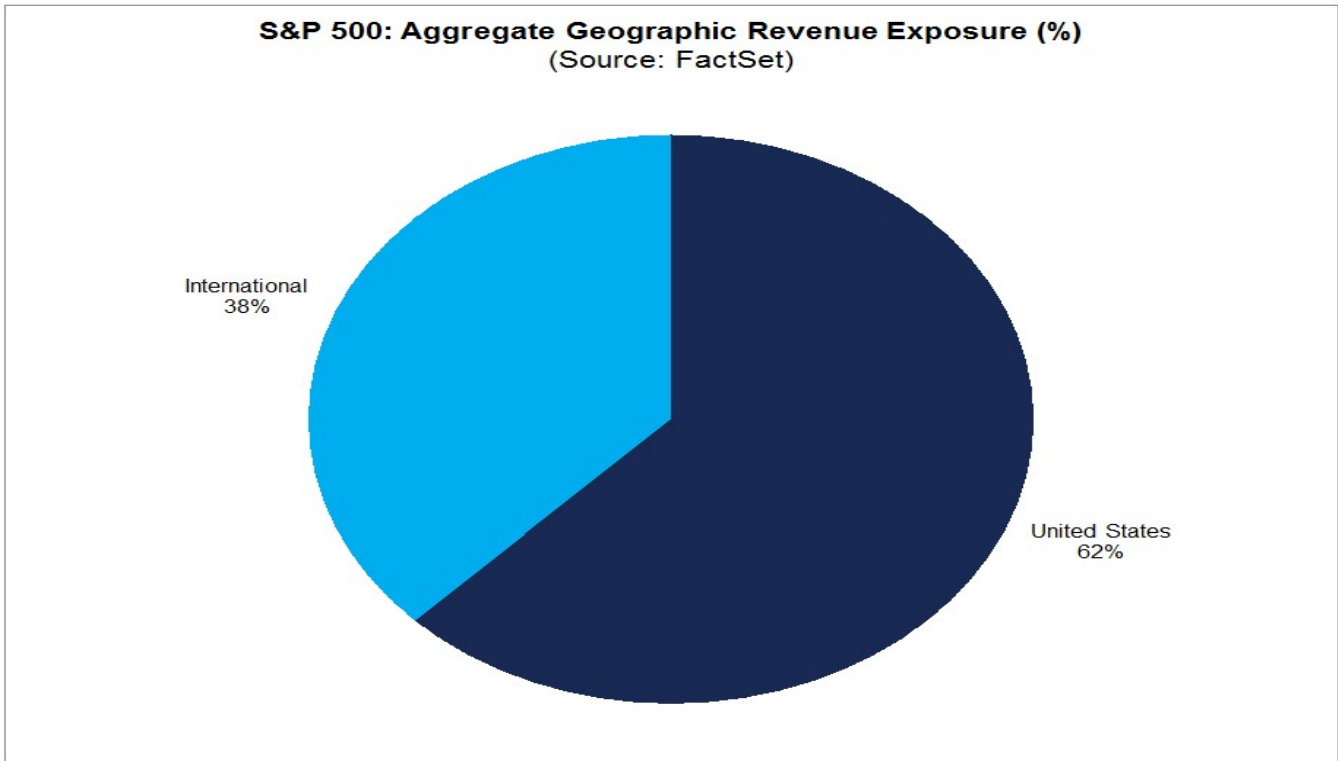
CY 2018: Growth



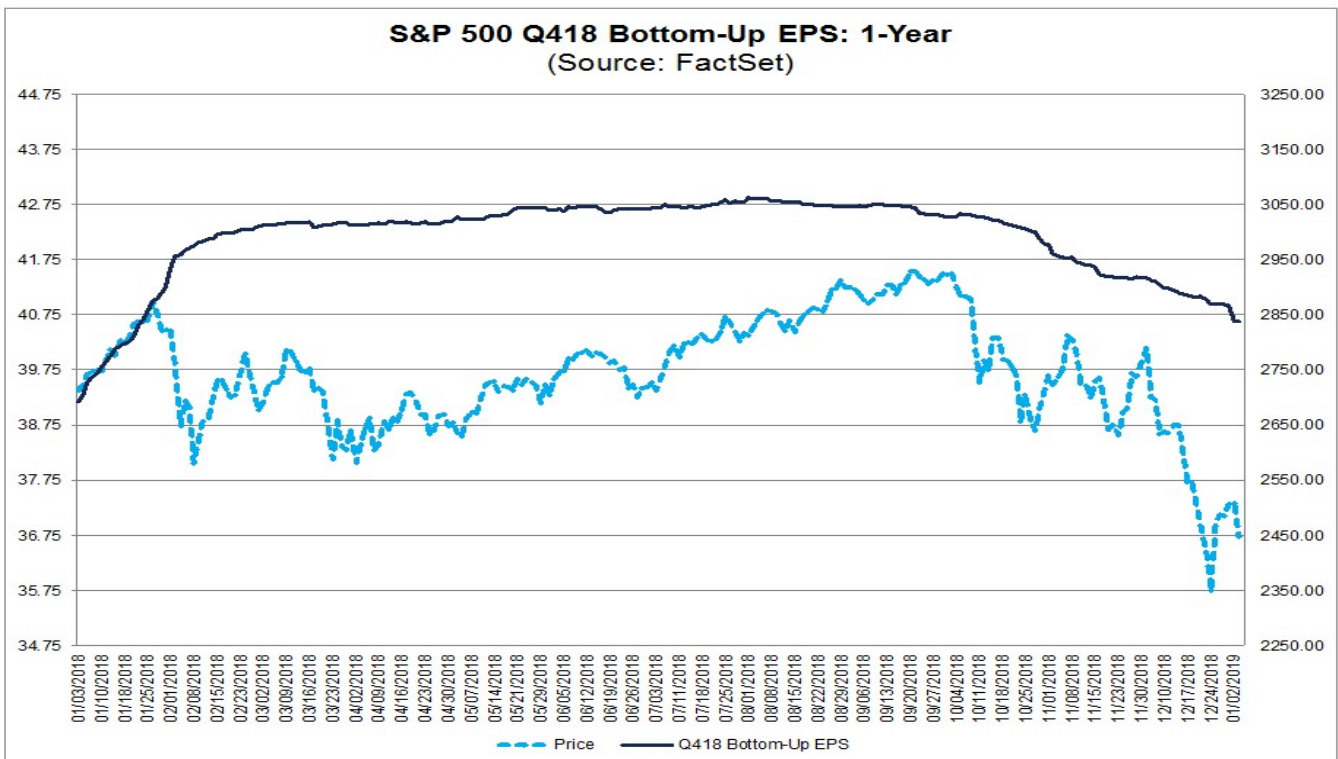
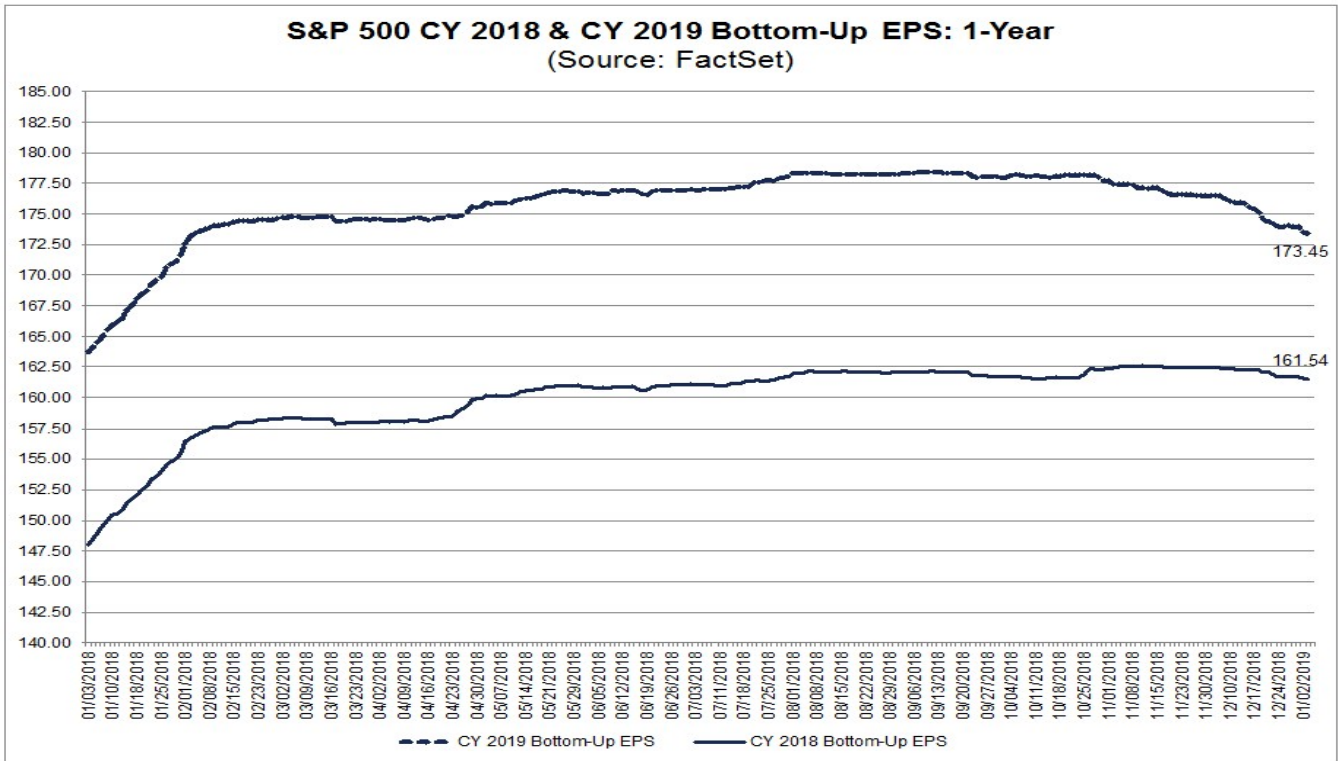
CY 2019: Growth



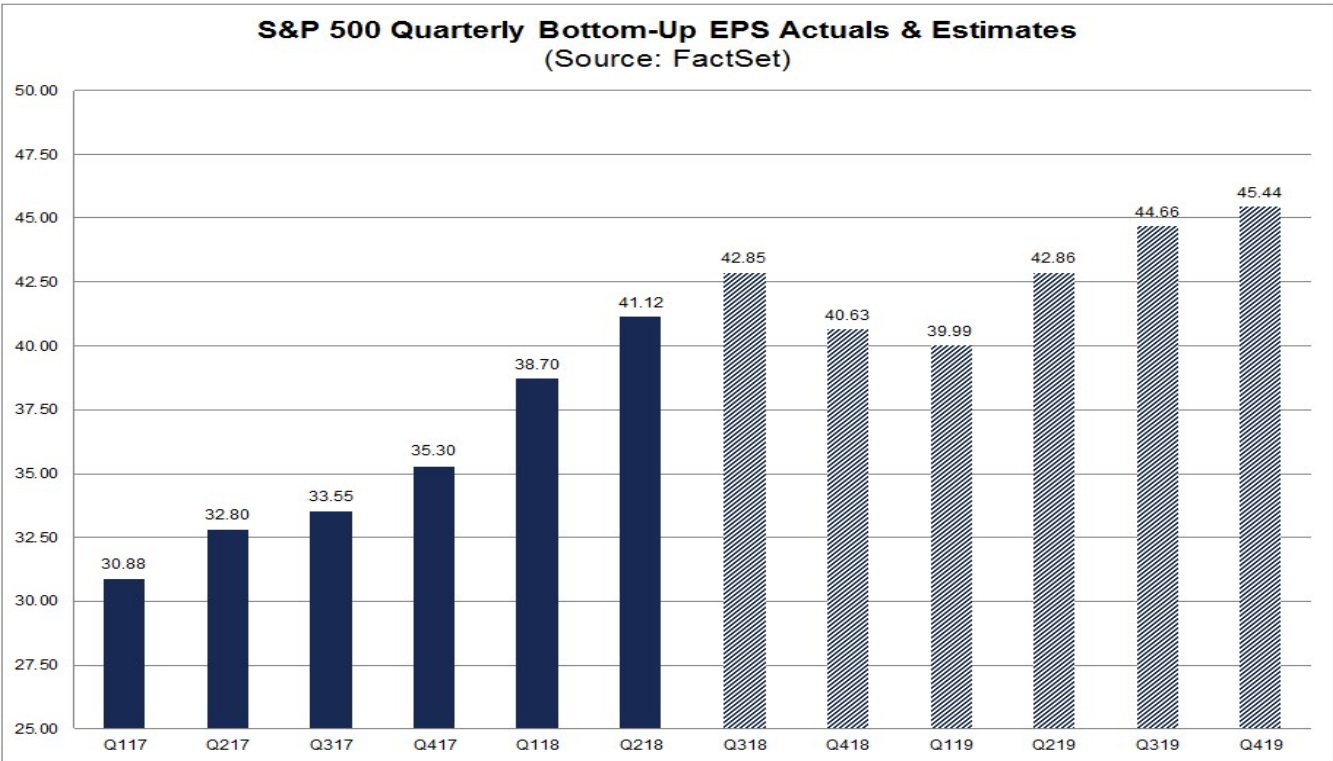
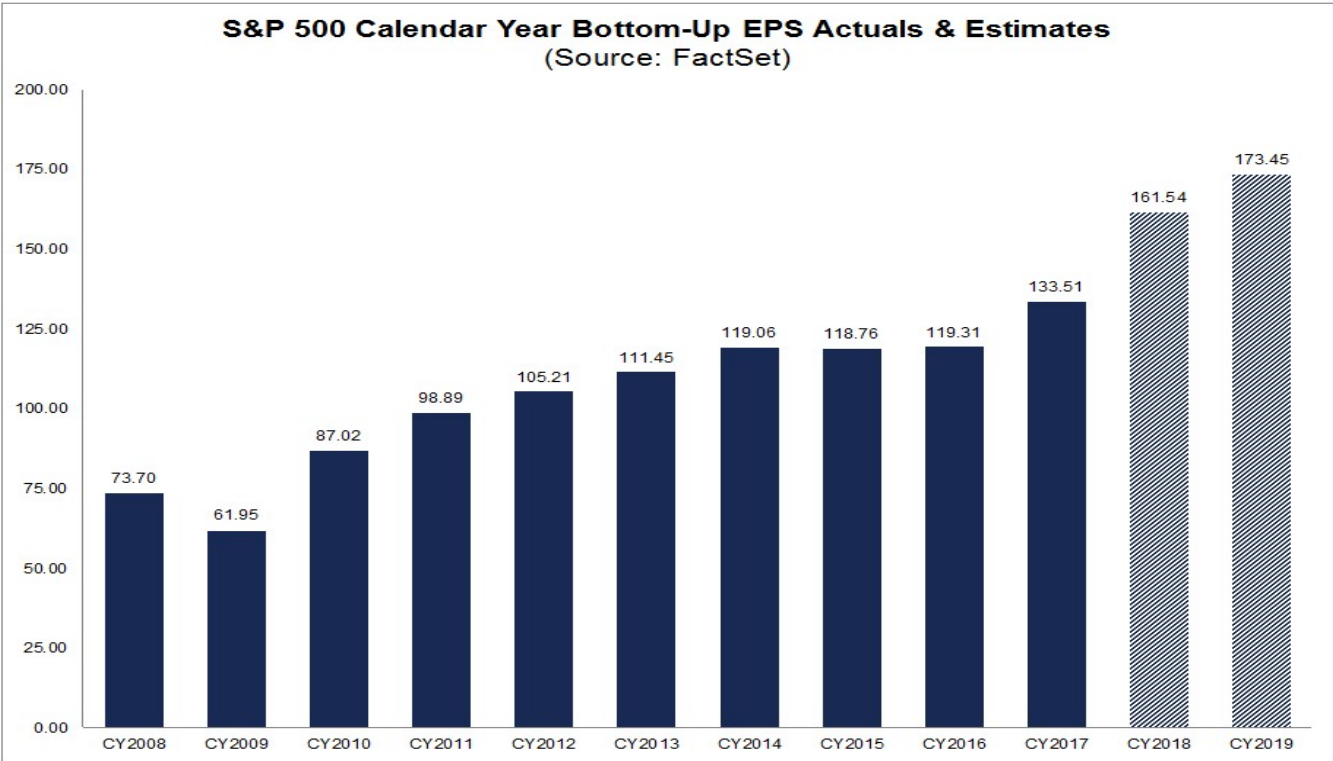
Geographic Revenue Exposure



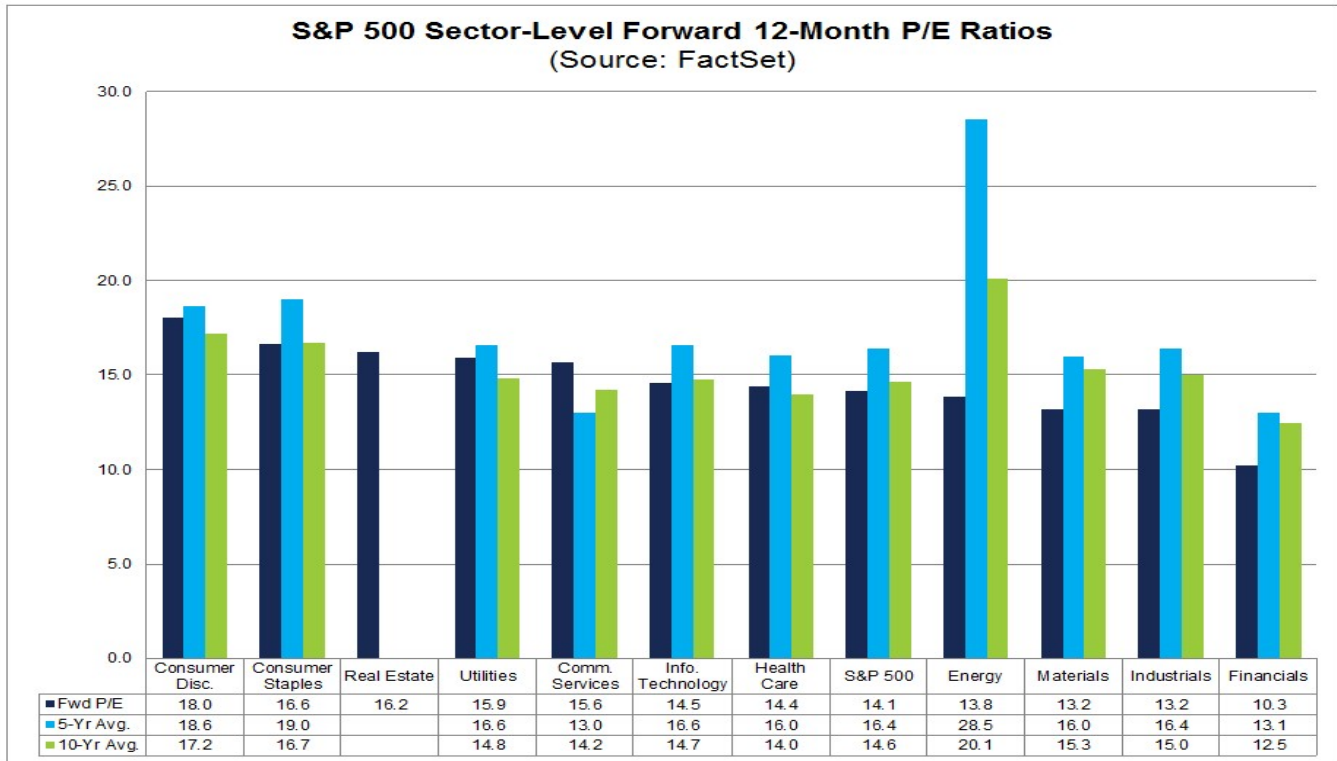
Bottom-up EPS Estimates: Revisions



Bottom-up EPS Estimates: Current & Historical

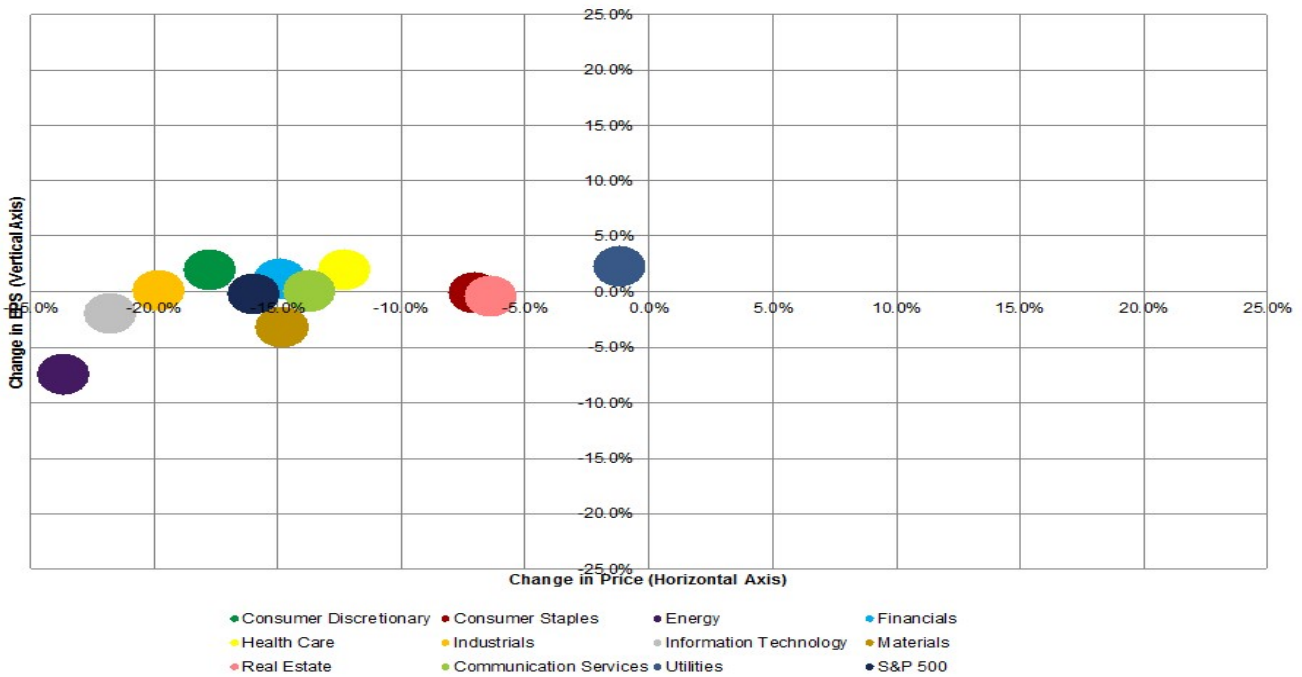


Forward 12M P/E Ratio: Sector Level

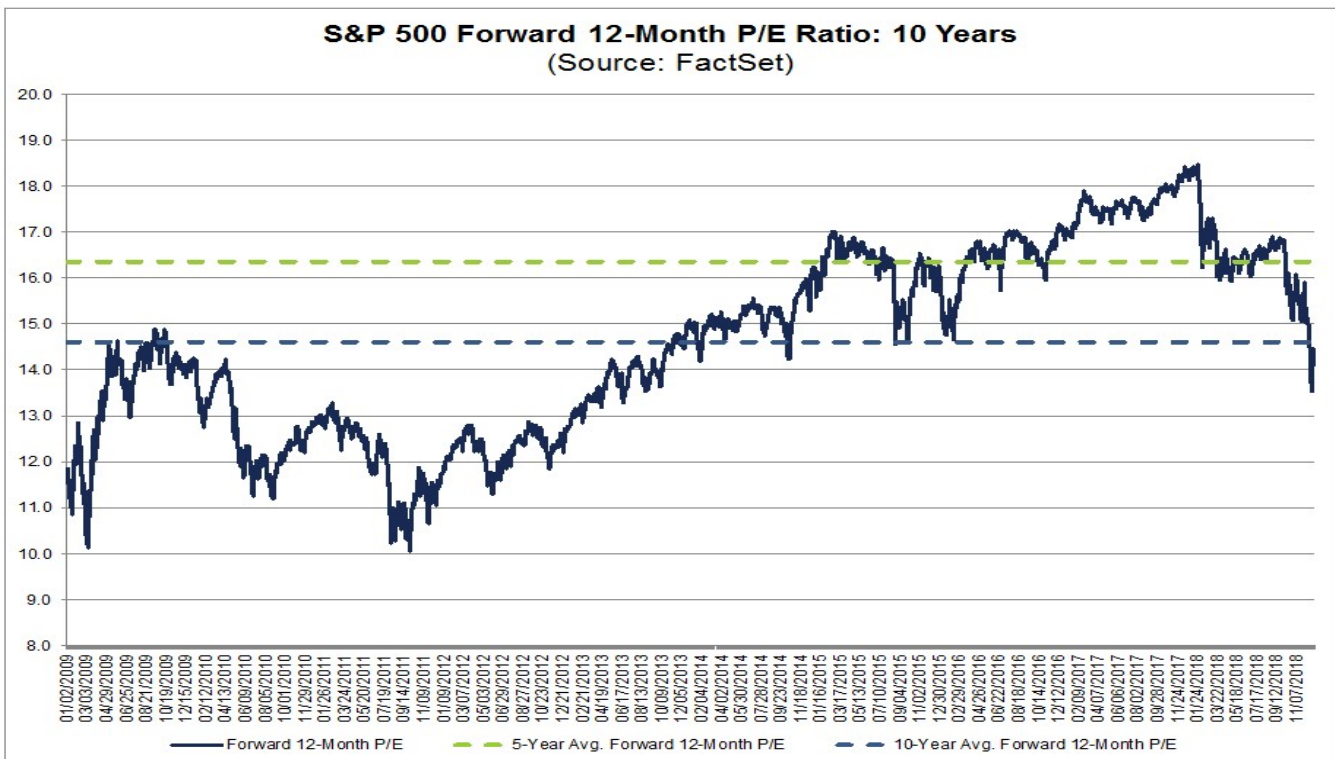
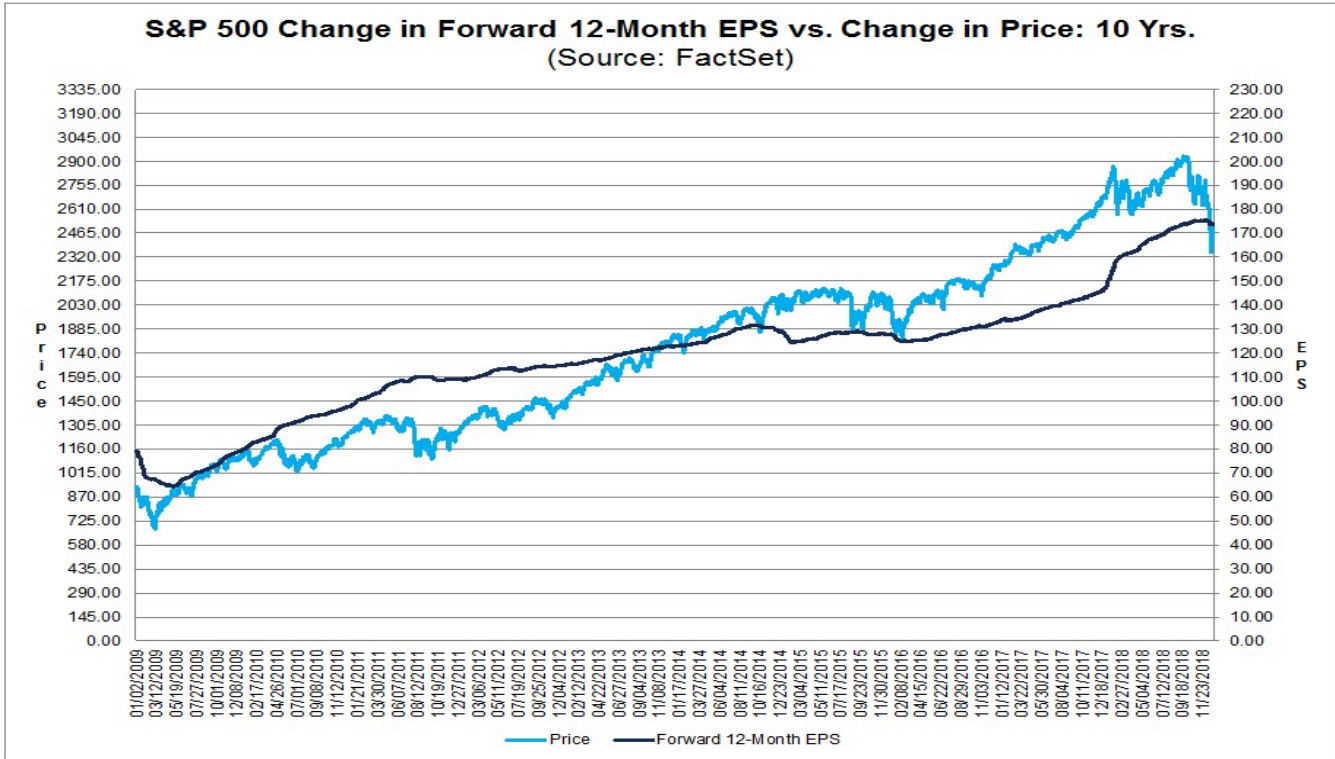


Sector-Level Change in Fwd. 12-Month EPS vs. Price: Since Sep 30

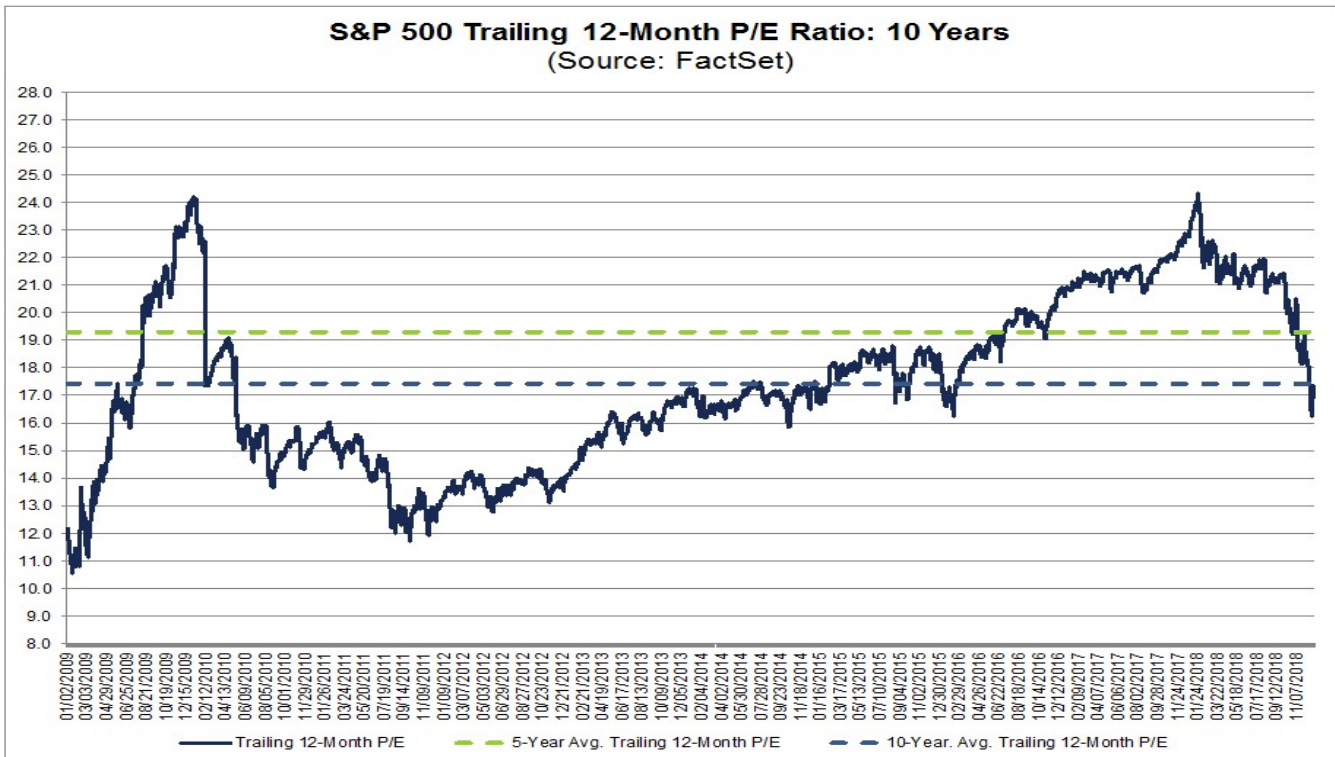
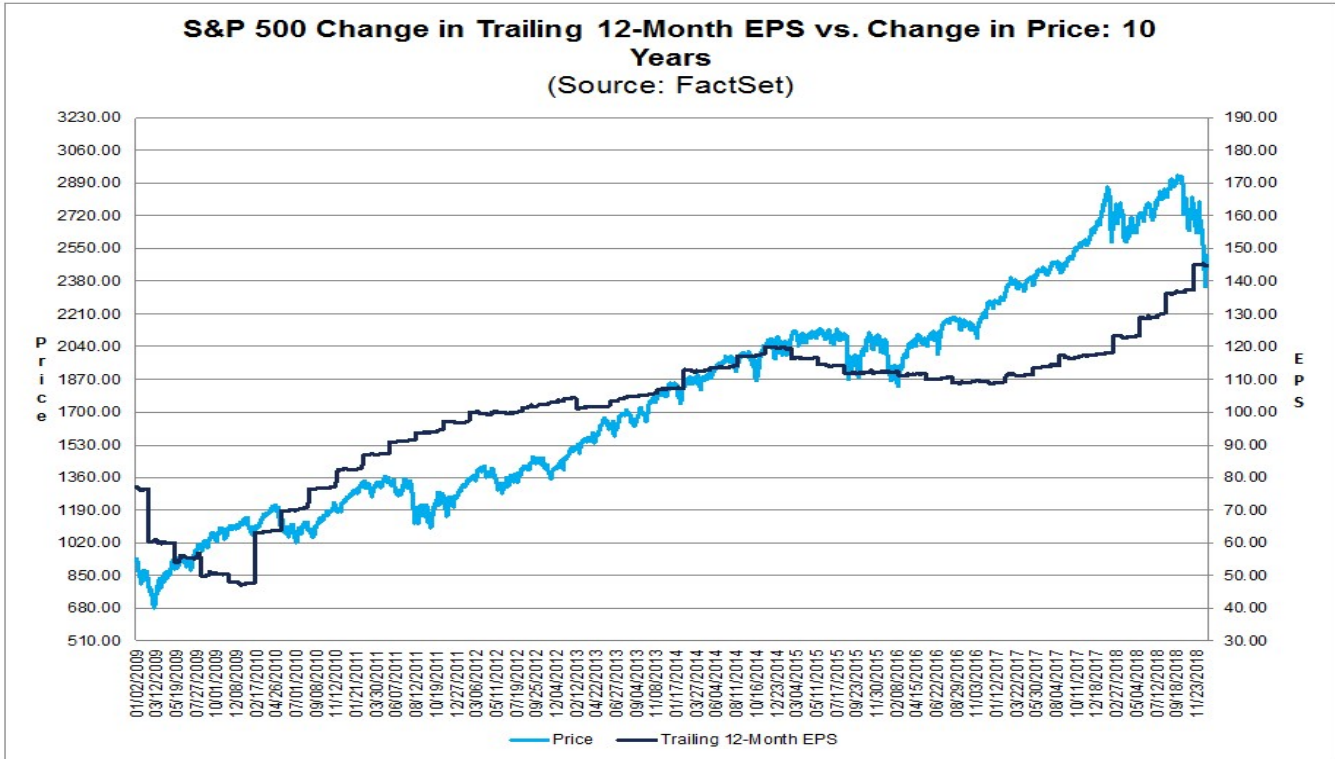
(Source: FactSet)



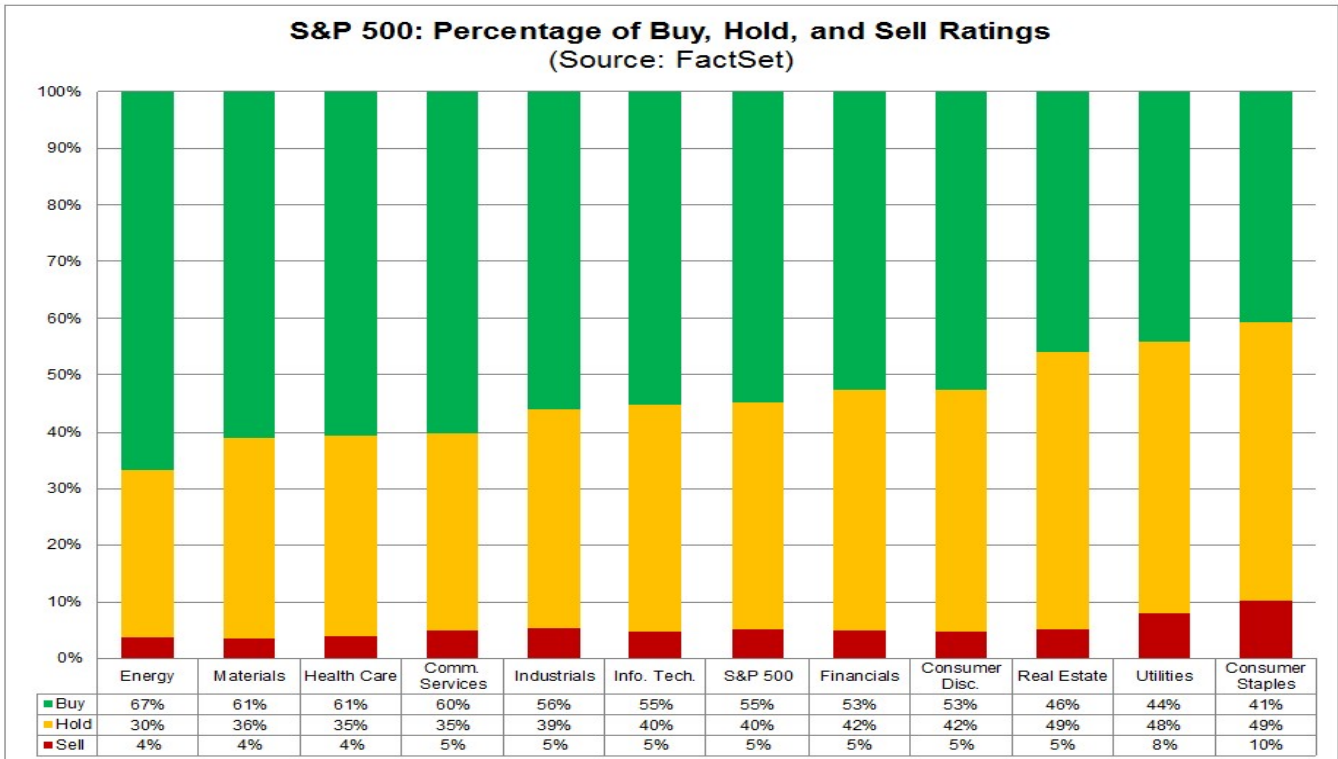
Forward 12M P/E Ratio: Long-Term Averages



Trailing 12M P/E Ratio: Long-Term Averages



Targets & Ratings



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