

Early Take on the Global Reporting Season

- Earnings appear resilient despite negative leading economic indicators.
- Consumer Discretionary and Industrials the most positive, while Materials and Energy the most negative.
- S&P/ASX 300 Index earnings trend looks negative going into August reporting period.

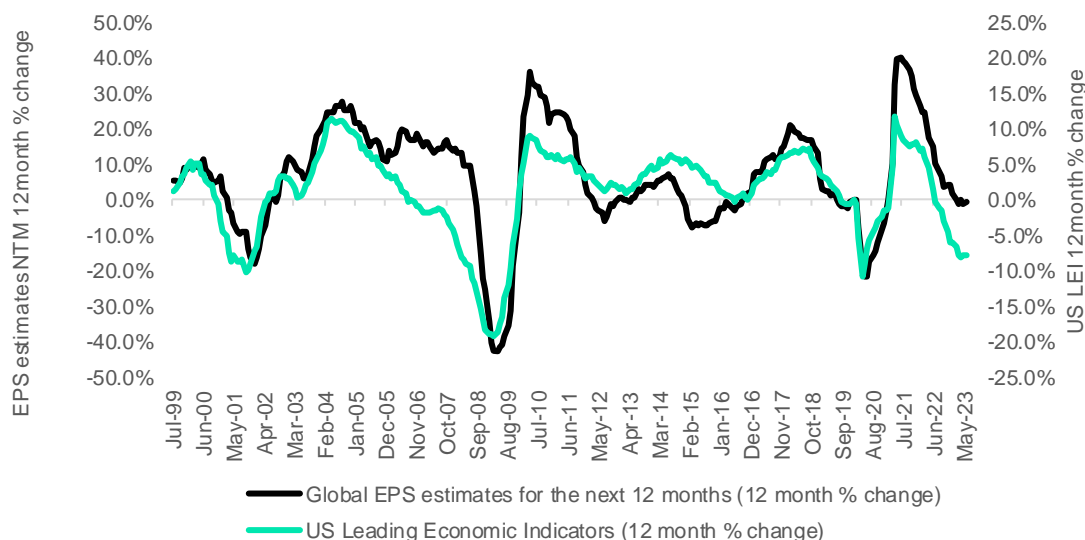


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US Leading Economic Indicators Continue to Point to Slower Earnings Growth

Figure 1 illustrates the link between changes in the Conference Board US leading economic index and changes in earnings expectations. The Leading Economic Index (LEI) is designed to provide an early indication of significant turning points in the business cycle and where the economy is heading in the near-term.¹ As shown in Figure 1, the LEI peaked in mid-2021 and has been negative since July 2022. The changes in earnings expectations has broadly tracked the changes in LEI. Earnings momentum peaked at a similar time to the peak in the LEI, and Earnings Per Share (EPS) estimates have been slowing ever since. In March 2023, the 12 month % change in EPS (NTM) turned negative for the first time since February 2020.

Figure 1: US Leading Economic Indicator (LEI) and Global Earnings Trends (EPS NTM)



Source: FactSet, State Street Global Advisors, The Conference Board, <https://www.conference-board.org/topics/us-leading-indicators>. The underlying earnings data is sourced from FactSet and represents market cap weighted returns and earnings per share for the representative indexes. EPS trends over time are based upon the 12 month % change in forecast EPS estimates.

With the continued negative trend in the leading economic indicators, many market participants have been expecting the global Q2 reporting season to result in a negative earnings trend. So far this has not materialised.

A Surprisingly Resilient Earnings Season So Far

At 30 June 2023, the EPS forecast for the next 12 months was \$175.3. After 3 weeks of company reports the 12 month forward EPS had improved to \$176.3 - an increase of 0.6%.² Figure 2 provides the break down across the sectors but key observations include:

- Consumer Discretionary and Industrials sectors were the most positive.
- Energy and Materials continue negative trend.
- Financials show the biggest trend reversal from negative to positive.

So far the MSCI World Index (MSCI World) has generated positive returns during reporting season (+1.6%), with all sectors generating positive returns (Financials being the most positive +3.9%). The change from negative to positive earnings trends for the next 12 months has contributed to Financials outperformance.

The positive returns in reporting season, on top of already positive returns for the first half of the year, have taken the market back to more expensive valuation levels. The last column in Figure 2 shows the Valuation PE (NTM) Percentile ranking compared to the last 20 years. The MSCI World now has a PE of 17.4x which is at the 86% percentile.

Figure 2: MSCI World Index EPS trends YTD and Since Reporting Season (30 June 2023)

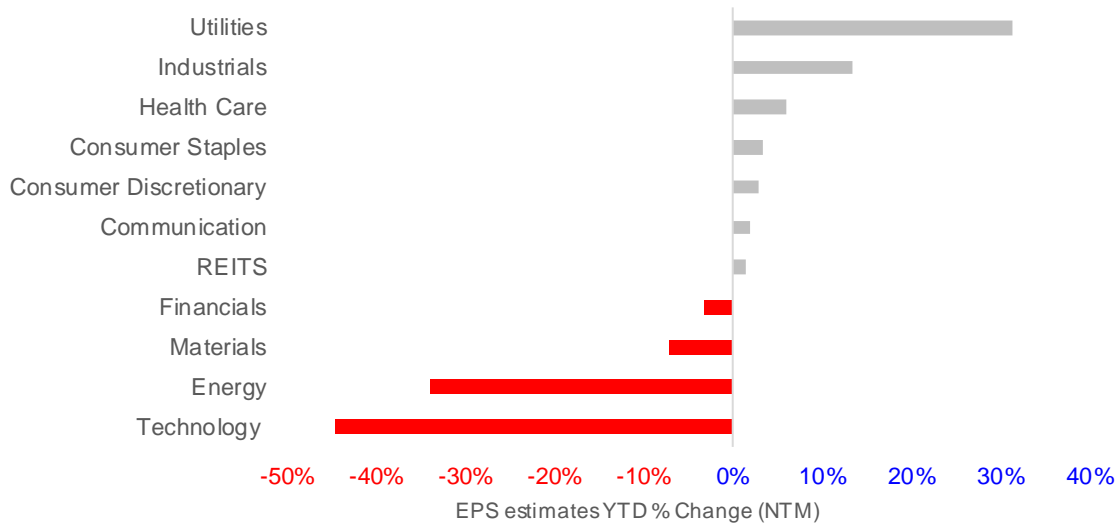
	Return USD YTD*	Return USD Reporting season**	EPS (NTM) Trend YTD*	EPS (NTM) Trend Reporting season**	Valuation Percentile***
MSCI World	14.0%	1.6%	0.8%	0.6%	86%
Communications	29.2%	0.2%	9.1%	1.4%	82%
Consumer Staples	2.1%	0.7%	4.3%	1.2%	70%
Utilities	-2.2%	2.8%	5.7%	1.5%	64%
Health Care	-0.3%	1.7%	0.4%	-0.3%	87%
Materials	4.1%	1.4%	-6.7%	-2.0%	69%
Industrials	13.8%	1.1%	1.8%	2.0%	88%
Financials	1.4%	3.9%	-4.5%	1.0%	39%
Energy	-6.4%	3.3%	-16.0%	-3.9%	12%
Consumer Discretionary	28.3%	0.5%	4.0%	2.4%	84%
Technology	38.6%	0.8%	3.2%	1.3%	86%

Source: FactSet, State Street Global Advisors. The underlying earnings data is sourced from FactSet and represents market cap weighted returns and earnings per share for the representative indexes. EPS trends over time are based upon the % change in forecast EPS estimates over the period stated. YTD* = 31 December 2022 to 30 June 2023. Reporting season** = 30 June 2023 to 21 July 2023. Valuation percentile*** = the percentile rank for the current market Price-to-earnings (PE) NTM compared to the last 20 years of month PE observations.

Earnings season is always a rich source of information for investors. While many focus on the reported results we are more interested in company forward guidance. As companies update investors on their operating environment and provide guidance, the investment analyst community adjust their forecasts for the company's future earnings. We can capture these trend changes by looking at the changes in the 12 month EPS forecasts.

In Australia, the next major set of company reports occur in August. While we have not seen many results so far, we can review the trends YTD to see how expectations have been evolving going into the upcoming reporting season. Figure 3 provides EPS trends YTD. The EPS trend for the S&P/ASX 300 Index at 21 July 2023 was -6.1%. At the end of June 2023 it was -4.7%. Despite an improvement in earnings globally the negative trend continued in Australia. The negative earnings trend for Materials and Energy observed in Australia, and overseas, has a bigger impact on the Australian equity market given the larger index weight towards these sectors. Financials have also been negative in Australia YTD, which also impacts a large proportion of the index and contributed to the more negative outlook for the S&P/ASX 300 Index. A major difference between Australian and overseas sectors occurred within Technology which was the most negative in Australia but positive across the MSCI World.

Figure 3: S&P/ASX 300 Index EPS trends YTD



Source: Factset, State Street Global Advisors. EPS trends YTD are calculated by measuring the % change from 31 December 2022 to 21 July 2023 in the estimates for sector earnings for the next twelve months (NTM).

The Bottom Line

It is still early in the global reporting season but so far the trend for most sectors is encouraging. Consumer Discretionary and Industrials had the most positive improvements, while the outlook for Materials and Energy remains negative. Within the Australian context, the negative YTD earnings trend for Materials, Energy and Financials is driving a more negative trend for the S&P/ASX 300 Index.

Footnotes

¹ The US Leading Economic Indicator includes both Financial components like credit, stock prices and interest rates as well as Non-financial economic variables such as expectations for business conditions, ISM new orders, building permits, average weekly hours in manufacturing, new orders and unemployment claims etc. See website for more details. <https://www.conference-board.org/topics/us-leading-indicators>

² Source: FactSet, State Street Global Advisors. From 30 June 2023 to 21 July 2023.

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Expiry Date: 31/07/2024