GLOBAL EARNINGS – OPEN FOR BUSINESS

Aneeka Gupta – Director, Macroeconomic Research
07 May 2021

The current earnings season sheds plenty of light on the outlook for global equity markets. This time last year, the world was thrown into disarray owing to the COVID-19 pandemic. Since then, we have seen lockdowns lifted as vaccination rollouts gather pace. In addition, the gradual resumption of economic activity, stimulative global fiscal plans, and the release of pent-up consumer demand are being reflected in first-quarter earnings results. As a result, the breadth of earnings revisions[1] has been strongest in the US, followed by Japan, Europe while Emerging Markets and China are turning more neutral[2].

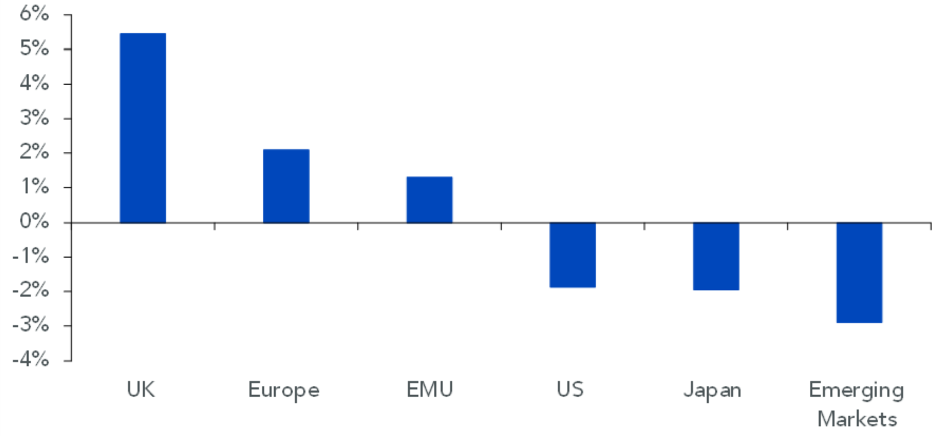
US earnings exceed expectations but margin pressure ahead

US first-quarter earnings have been exceptional, to say the least. Earnings Per Share (EPS) growth is tracking a 46% increase compared to pre-season growth expectations of 24%[3]. Financials and Discretionary sectors are leading the gains. Energy has reversed into a gain from an expected year-on-year decline, helped by higher oil prices this year. First-quarter sales are expected to increase 8.9% versus consensus estimates of 6.1%. Materials, Discretionary, Technology and communications sectors are on track to post double-digit sales growth among the 71.4% of companies reported so far. Amid a strong first-quarter earnings report, forward-looking EPS estimates are being revised upwards led by financials, energy, materials and communication sectors. We caution that while the outlook for earnings remains strong, there are risks on the horizon emanating from the proposal of higher corporate taxes, which are central to the Biden Administration's proposed infrastructure package. In addition, the combination of slower revenue growth coupled with rising costs could squeeze margins unless corporations are willing to pass on the costs are passed on to the end consumer.

A strong but expected beat in Europe

European companies on the broad EuroStoxx 600 Index are heading for their best earnings season. First-quarter results in Europe tracked so far point to a decisive headline beat with weighted earnings at 25%, currently well ahead of expectations. In addition, there has been a very large breadth of Earnings Per Share (EPS) beats compared to the prior quarter last year, marking the broadest beat since 2009[4]. Despite the record rate of beats, price reaction on the day of results has been negative, which suggests most of the good news is already priced in. The breadth of sales beats has been narrower, the shortfall was evident in the energy and utilities sector that suffered due to weak demand during lockdowns. Europe is the only region where earnings revisions are still higher than sales revisions, suggesting fewer signs of margin pressure than in other regions in the current period.

Figure 1: Gap between 12M Earnings & Sales Revision Ratio (%)



Source: IBES, Bloomberg, WisdomTree, data available as of close 07 May 2021. EMU stands for Economic and Monetary Union or Eurozone.

Historical performance is not an indication of future performance and any investments may go down in value.

Among the 70% of the companies on the EuroStoxx 600 Index that have reported earning, cyclicals have fared better than defensive counterparts. The outperformance among Industrials and materials were driven by restructuring programs. While a rebound in demand helped consumer discretionary and technology sectors. Lower than expected loan loss provisions (16.3Bn vs 20.6Bn)[1] benefited the financial sector. Financials have delivered the strongest earnings beats 48% across all sectors so far[1]. Optimism for recovery was evident in company earnings announcements in sharp comparison to the prior quarter. Financials were encouraging, with banks committing to resuming dividends while insurers are hoping to benefit from price increase and rising bond yields. One way to capture the potential opportunity in Industrials, Materials and Financials is via European small-caps see European Small Caps.

Japan moving in the right direction

Among the 41% of companies reported in Japan[5], Japanese companies are reporting a weighted earnings surprise of 5.4% and a net beat of 20%, which is relatively modest compared to the average 37% quarterly beat in the prior three quarters. Stock reaction has been negative despite the strong beat of earnings results. Japan's 12month forward revision breadth remains positive, helped by a weaker Yen and improving economic outlook. The results so far highlight Energy, Materials, Auto parts and Electronic Components have shown beats while pharmaceuticals sector has been relatively weak.

China A-shares earnings season slight deceleration

China A-shares[6] reported recent fourth quarter (4Q20) earnings that were notably weaker than the previous quarter (3Q 20), where reported earnings were in line with consensus. Financials, consumer discretionary, and consumer staples were among the sectors seen exceeding consensus expectations. However, communication services and IT missed consensus earnings forecasts. Industrials were also negatively impacted owing to the weak performance of the big three Chinese airline companies. After being in positive territory since August 2020, earnings estimate revision breadth for A-shares have started to decelerate in sharp comparison to other regions – the US, Europe and Japan.

Nevertheless, we remain positive on the earnings growth trajectory for the rest of 2021 as we expect to see a resumption of economic activity driven by the Chinese consumer and robust manufacturing CAPEX. The Chinese economy grew at 18.3% in the first quarter of 2021, we expect growth rates to normalise around 7% for the rest of the second half (H2) of 2021. Uncertainties linked to policy tightening by the Peoples Bank of China (PBOC) in H2, ongoing internet regulation, liquidity and valuations suggest a more cautious outlook in the near term.

Sources

[1] Breadth of earnings revisions represents the trailing 3 months moving average of earnings revisions

[2] IBES, Factset, WisdomTree

[3] Among the three-quarters of companies on the S&P 500 Index

[4] Bloomberg

View the online version of this article here.

Important Information

Marketing communications issued in the European Economic Area ("EEA"): This document has been issued and approved by WisdomTree Ireland Limited, which is authorised and regulated by the Central Bank of Ireland.

Marketing communications issued in jurisdictions outside of the EEA: This document has been issued and approved by WisdomTree UK Limited, which is authorised and regulated by the United Kingdom Financial Conduct Authority.

WisdomTree Ireland Limited and WisdomTree UK Limited are each referred to as "WisdomTree" (as applicable). Our Conflicts of Interest Policy and Inventory are available on request.

For professional clients only. The information contained in this document is for your general information only and is neither an offer for sale nor a solicitation of an offer to buy securities or shares. This document should not be used as the basis for any investment decision. Investments may go up or down in value and you may lose some or all of the amount invested. Past performance is not necessarily a guide to future performance. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

The application of regulations and tax laws can often lead to a number of different interpretations. Any views or opinions expressed in this communication represent the views of WisdomTree and should not be construed as regulatory, tax or legal advice. WisdomTree makes no warranty or representation as to the accuracy of any of the views or opinions expressed in this communication. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

This document is not, and under no circumstances is to be construed as, an advertisement or any other step in furtherance of a public offering of shares or securities in the United States or any province or territory thereof. Neither this document nor any copy hereof should be taken, transmitted or distributed (directly or indirectly) into the United States.

Although WisdomTree endeavours to ensure the accuracy of the content in this document, WisdomTree does not warrant or guarantee its accuracy or correctness. Where WisdomTree has expressed its own opinions related to product or market activity, these views may change. Neither WisdomTree, nor any affiliate, nor any of their respective officers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this document or its contents.