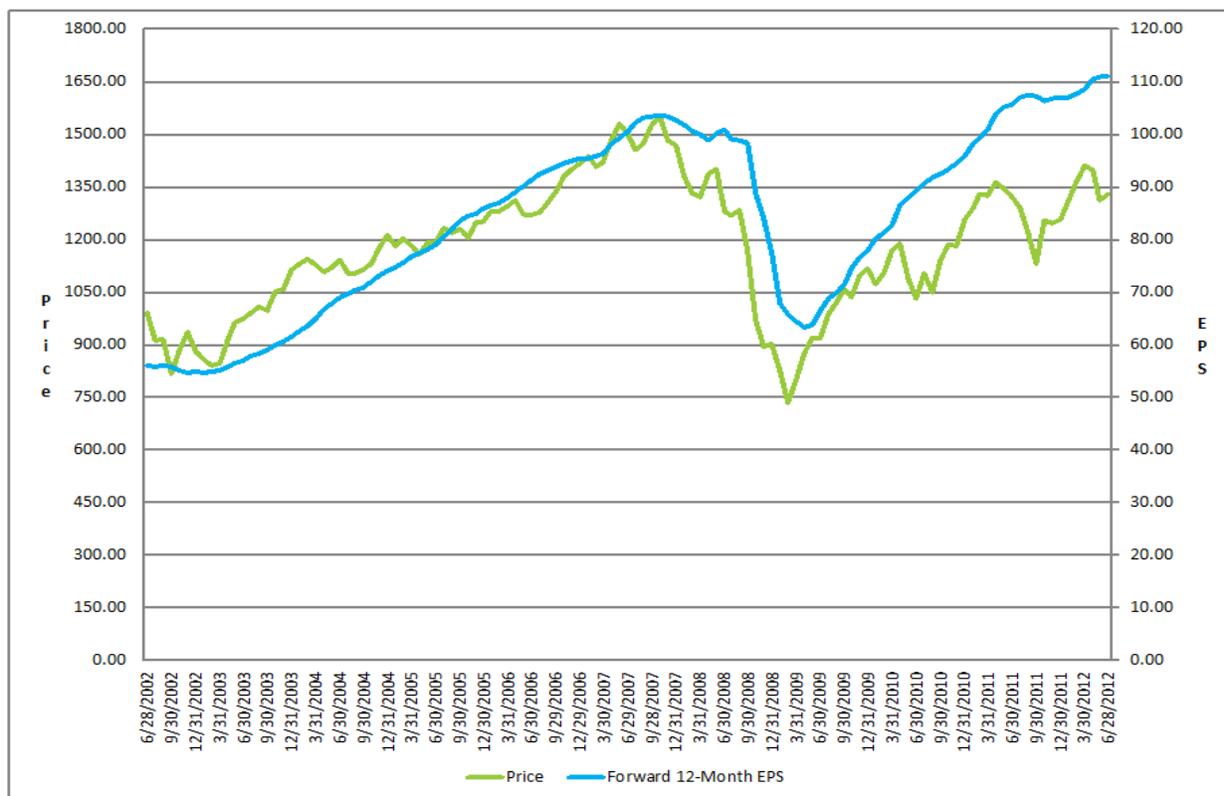


## Key Metrics

- + **Earnings Growth:** The estimated earnings growth rate for Q2 2012 is 3.0%. The Financials (51.2%) sector is expecting the highest earnings growth rate for the quarter while the Energy (-19.3%) and Materials (-11.9%) sectors are expecting the lowest earnings growth rates.
- + **Earnings Revisions:** Since March 31, the blended earnings growth has decreased to 3.0% from 6.4%. The Energy and Financials sectors have recorded the largest downside revisions to earnings estimates during this time.
- + **Earnings Guidance:** For the current fiscal quarter, 74 companies have issued negative EPS guidance and 28 companies have issued positive EPS guidance.
- + **Valuation:** The current 12-Month forward P/E ratio is 12.0. This P/E ratio is below the average forward 12-Month P/E ratio over the past 10 years (14.4).
- + **Earnings Scorecard:** Of the 23 companies that have reported earnings to date for Q2 2012, 70% have reported earnings above the mean estimate.

S&P 500 Forward 12-Month EPS vs. Price: 10-Year



All data published in this report is available on FactSet. Please contact media\_request@factset.com or 1-877-FACTSET for more information.

## Topic of the Week:

### Q2 EPS Guidance: More Negative, Fewer Positive than Recent Quarters

With the second quarter ending this week, it marks a good time to analyze guidance data for the second quarter. To date, 102 companies in the S&P 500 have issued quarterly EPS guidance for the second quarter. Of these 102 companies, 74 have issued negative EPS guidance and 28 have issued positive EPS guidance.

How do these numbers compare to recent quarters? Are they more negative? Are they more positive?

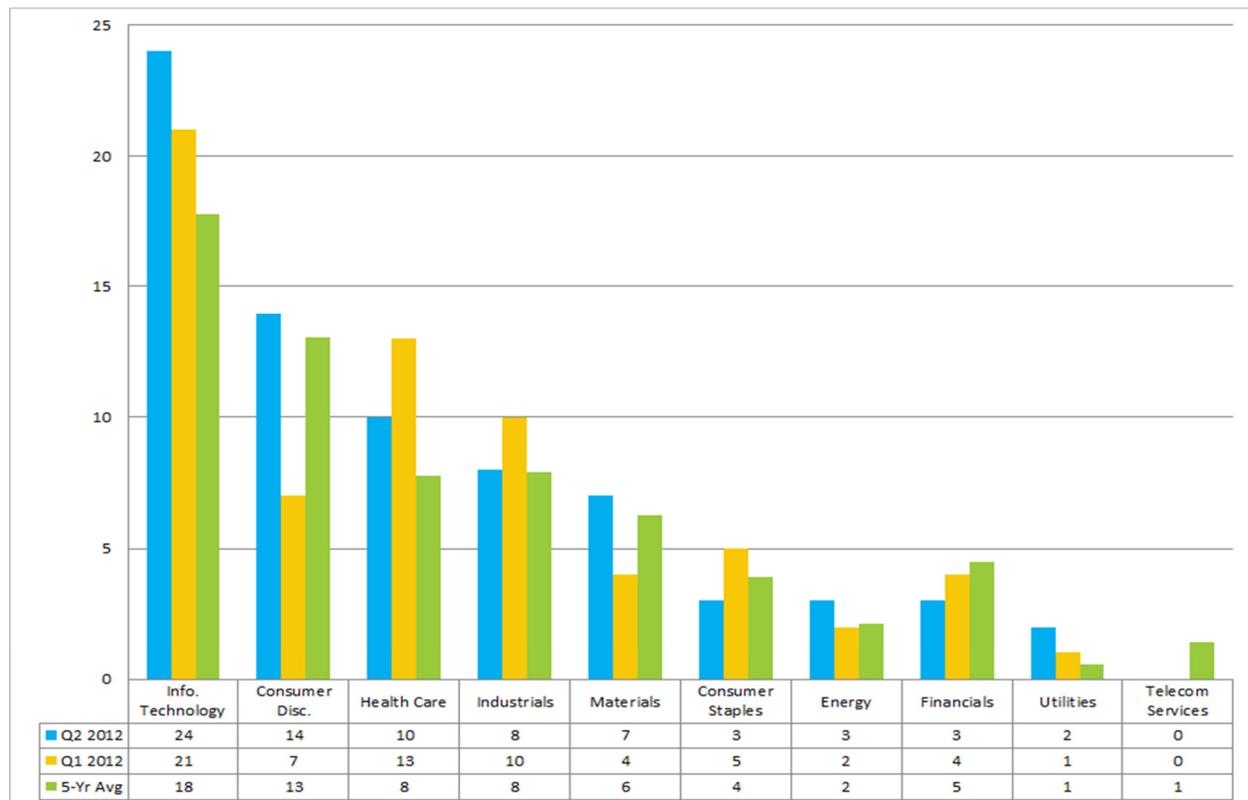
Compared to Q1 2012, these numbers are definitely more negative. For Q1 2012, 111 companies issued EPS guidance. Of these 111 companies, 67 issued negative EPS guidance and 44 issued positive EPS guidance. The Consumer Discretionary sector has witnessed the largest increase (+7) in the number of companies issuing negative EPS guidance and the largest decrease (-9) in the number of companies issuing positive EPS guidance in Q2 2012 relative to Q1 2012.

Compared to the trailing five-year average, the guidance numbers for Q2 2012 are also more negative. On average over the past five years, 106 companies have issued EPS guidance. Of these 106 companies, 65 issued negative EPS guidance and 41 issued positive EPS guidance on average.

It is interesting to note there has been a significant decline in the number of companies issuing positive guidance in Q1 2012 relative to recent quarters. If the final number of companies issuing positive guidance is 28, it will mark the first time the number has finished below 30 since Q2 2006 (29).

For more detailed content on guidance, please see our new report going out later today called "Guidance Monthly."

Number of S&P 500 Companies Issuing Negative EPS Guidance: Q212, Q112 & 5-Yr Average



## Q2 2012 Earnings Season: Overview

### Estimated Earnings Growth Rate Dropped Slightly This Week to 3.0% from 3.1%.

The estimated earnings growth rate for the second quarter currently stands at 3.0%, slightly below last week's estimate of 3.1%. Downward revisions to estimates for companies in the Financials (including Goldman Sachs and Morgan Stanley) sector were mainly responsible for the small decline. The mean EPS estimate for Goldman Sachs dropped to \$1.61 from \$1.93. The mean EPS estimate for Morgan Stanley fell to \$0.39 from \$0.46. Overall, the estimated earnings growth rate for the Financials sector decreased to 51.2% from 53.5% during the week.

Since the start of the second quarter (March 31), the earnings growth rate for the index has declined to 3.0% from 6.4%. Nine of the ten sectors have recorded a decrease in earnings growth rates during this time, led by the Energy and Financials sectors. The Telecom Services sector is the only sector that has witnessed a slight increase in projected earnings growth since March 31.

### Highest Earnings Growth: Financials, Industrials, & Information Technology.

The estimated earnings growth rate for Q2 2012 is 3.0%. If this is the final growth rate, it will mark the 11<sup>th</sup> consecutive quarter of earnings growth for the index. Overall, four of the ten sectors are predicted to see year-over-year earnings growth for the quarter. Of these four sectors, the Financials, Industrials, and Information Technology sectors are expecting the highest earnings growth for the quarter.

#### Financials Sector: Easy Comparisons to Year-Ago Losses Boost Bottom-Line Growth.

The Financials sector is predicted to have the highest earnings growth (51.2%) of all ten sectors. However, this sector is only projected to see revenue growth of 3.2%. Most of the companies that are projected to see the highest dollar-level increases in earnings in this sector reported large losses in the year-ago quarter. Bank of America is expected to be the largest contributor to earnings growth in the sector, mainly due to an easy comparison to a year-ago EPS loss (-\$0.90). If Bank of America is excluded, the estimated earnings growth rate for the Financials sectors falls to 6.8%. In addition to Bank of America, Morgan Stanley, Allstate, and Travelers all reported losses in the year-ago quarter and are now predicted to be large contributors to earnings growth for the sector in Q2 2012.

#### Industrials Sector: Solid Growth across the Sector Led by Machinery and Conglomerates

The Industrials sector has the second highest earnings growth rate at 6.7% and the third highest revenue growth rate at 6.1%. Ten of the twelve industries in this sector are predicted to see earnings growth, while five of these ten industries are expected to report double-digit growth. Companies in the Machinery (such as Caterpillar, Deere, and Paccar) and Industrial Conglomerates (such as General Electric and Danaher) industries are expected to be the largest contributors to earnings growth for the sector. In Q1 2012, a number of companies in this sector cited a better than expected performance in the U.S. as a reason for strong earnings growth for the quarter, offsetting weaker results globally. Will companies in this sector continue to see this type of performance in the U.S. in Q2 2012?

#### Information Technology Sector: Apple

The Information Technology has the third highest earnings growth rate (3.6%) and the second highest sales growth rate (6.4%) of all ten sectors. However, almost all of this growth is due to Apple. Excluding Apple, the earnings growth rate for the Information Technology sector falls to -2.0%, and the sales growth rate falls to 3.2%. Apple is part of the Computers & Peripherals industry, which has the highest earnings growth rate (18.1%) of any industry in the sector. The Internet & Software Services (13.0%) and Communications Equipment (10.7%) industries are also predicted to see double-digit earnings growth for the quarter. The Semiconductor & Semiconductor Equipment industry is expected to see the lowest earnings growth (-20.4%) of all eight industries in the sector.

### **Excluding Bank of America, Earnings Growth Falls to -1.7%**

Not only is Bank of America the largest contributor to earnings growth for the Financials sectors, it is also the largest contributor to earnings growth for the entire S&P 500. Excluding Bank of America, the earnings growth rate for the index would fall to -1.7% from 3.0%. Bank of America is predicted to report EPS of \$0.16 compared to the year-ago actual EPS of -\$0.90.

### **Lowest Earnings Growth Predicted For Commodity-Based Sectors: Energy & Materials**

The Energy and Materials sectors are expected to see the lowest earnings growth of all ten sectors in Q2 2012. It appears both sectors have been impacted by the recent sharp decline in commodity prices. The weekly price for Brent Crude (ICE/\$bbl) has declined 27.4% since the start of the quarter (to \$89.23 from \$122.88), while the weekly price of the Reuters/Jefferies CRB Index has fallen 11.9% (to 271.81 from 308.46) during this time. Both the average weekly price of Brent Crude and the average weekly price of the Reuters/Jefferies CRB index for Q2 2012 to date are below their average weekly prices in the year-ago quarter.

The Energy sector is predicted to see the lowest earnings growth (-19.3%) and lowest sales growth (-14.0%) of all ten sectors. Within the sector, the Energy Equipment & Services industry is expecting to report earnings growth of 8.2%, while the Oil, Gas, & Consumable Fuels industry is projected to report an earnings decline of 22.2%.

The Materials sector is expected to see the second lowest earnings growth (-11.9%) and the third lowest revenue growth (3.2%) of all ten sectors. Three of the five industries are projected to see substantial decreases in earnings for the quarter. The Metals & Mining (-37.3%) industry is the largest contributor to the expected decline in earnings for the sector.

### **EPS Guidance: More Negative Relative to Q1**

Of the 104 companies that have issued EPS guidance for the current quarter, 74 have issued projections below the mean EPS estimate and 28 have issued projections above the mean EPS estimate. For Q1 2012, 67 companies issued projections below the mean EPS estimate and 44 companies issued projections above the mean EPS estimate. The Consumer Discretionary sector has seen the largest increase in the number of companies issuing negative EPS preannouncements and the largest decrease in the number of companies issuing positive EPS preannouncements in Q2 2012 relative to Q1 2012.

### **Revenue Growth: 9 of 10 Sectors Projected to Report Growth**

In terms of revenues, the estimated growth rate stands at 1.5%, down from an estimate of 3.4% at the start of the quarter. The Energy sector has witnessed the largest cuts to sales estimates since March 31. If 1.5% is the final growth rate for the quarter, it will mark the 11<sup>th</sup> consecutive quarter of revenue growth for the index. Nine of the ten sectors are expected to report sales growth for the quarter. The only sector predicted a report decline in sales is Energy (-14.0%).

### **Companies Continue to Face Higher Costs**

Eight of the ten sectors in the index are projected to report higher revenue growth than earnings growth for the quarter, which indicates that companies are having difficulty converting sales growth to earnings growth in Q2 2012. Higher costs are a likely cause of this dichotomy.

### **Revenue Increase, Earnings Decrease for 104 Companies**

At the company level, 104 companies are projected to report growth in sales but a decline in earnings in Q2 2012. If 104 is the final number of companies, it would be the highest number recorded since Q3 2008 (115), and would reflect a 44% increase compared to the number of companies recording this difference in the year-ago quarter (72). At the sector-level, the Consumer Discretionary (20) and Financials (17) sectors have the largest number of companies with this difference.

It is interesting to note that the Financials sector is actually one of the two sectors in which earnings growth (51.2%) is expected to outpace revenue growth (3.2%), though this is due to some companies in the sector benefitting from easy year-ago earnings comparisons. The estimated net profit margin for the index (including Financials) is 9.4%, which is equal to the average net profit margin recorded over the past four quarters (9.4%).

### Global Economic Slowdown

Companies in the index will likely see lower revenue growth outside of the U.S. relative to recent years due to slowing economic growth in emerging markets and Europe.

*"As expected, the International segment operating loss was driven primarily by lower revenue in Europe and China and increased competitive conditions in Europe." -Best Buy (May 22)*

### China and Emerging Markets

Economic growth in countries in emerging markets has been decreasing over the past year. According to FactSet Economics, three of the four "BRIC" countries have recorded slower GDP growth during this time. For Q1 2011, China, India and Brazil recorded GDP growth of 9.7%, 9.7% and 4.1%, respectively. By Q1 2012, GDP growth rates for China, India, and Brazil had fallen to 8.1%, 4.1% and 0.7%.

### Europe and F/X Rates

Economic growth in Europe has also fallen over the past year. In Q1 2011, the European Union recorded GDP growth of 2.4%. By Q1 2012, GDP growth in the European Union had fallen to 0.1%.

The continuing weakness in Europe is contributing to another factor that will have a negative impact on revenue and earnings growth in Q2 2012: less favorable foreign exchange rates. In 2011, many companies recorded a boost to revenues due to the weakness of the dollar relative to the Euro and other currencies. However, the ongoing weakness in Europe has led to the dollar gaining strength relative to the Euro in recent months. In Q2 2011, one Euro was equal to about \$1.44 U.S. dollars on average (weekly basis). For Q2 2012 to date, one Euro is equal to about \$1.28 U.S. dollars on average (weekly basis).

Companies have commented on the negative impact of foreign exchange rates on revenues.

*"Foreign exchange has been a strong headwind. When we set our initial guidance for this fiscal year, we expected foreign exchange to add two to three points to top-line growth. This range has declined by three to four percentage points, which equates to roughly \$3 billion in sales or a negative earnings impact of \$0.15 to \$0.18 per share." -Procter & Gamble (Jun. 20)*

### Analysts Take Down 2<sup>nd</sup> Half Estimates; Double-Digit Growth Still Projected for Q4

In addition to lowering estimates for Q2 2012, analysts also have reduced earnings growth expectations for Q3 2012 (to 1.1% from 4.1%) and Q4 2012 (to 13.5% from 15.5%) since March 31.

Despite the decline in earnings estimates for Q4 2012, analysts are still calling for double-digit growth (13.5%) for the quarter. Five of the ten sectors are predicted to report double-digit earnings growth, led by the Materials (32.3%) and Financials (27.8%) sectors.

### Valuation: Forward P/E Below 10-Year Average, Down Since March 31

The current forward 12-month P/E ratio of 12.0 is well below the prior ten-year average forward 12-month P/E ratio of 14.4, and is below the 13.0 P/E ratio recorded at the start of the second quarter (March 31). The P/E ratio has decreased during this time due to a decline in the price of the index (down 5.6% since March 31), combined with an increase (2.2%) in the forward 12-Month EPS estimate for the index (to 111.01 from 108.67).

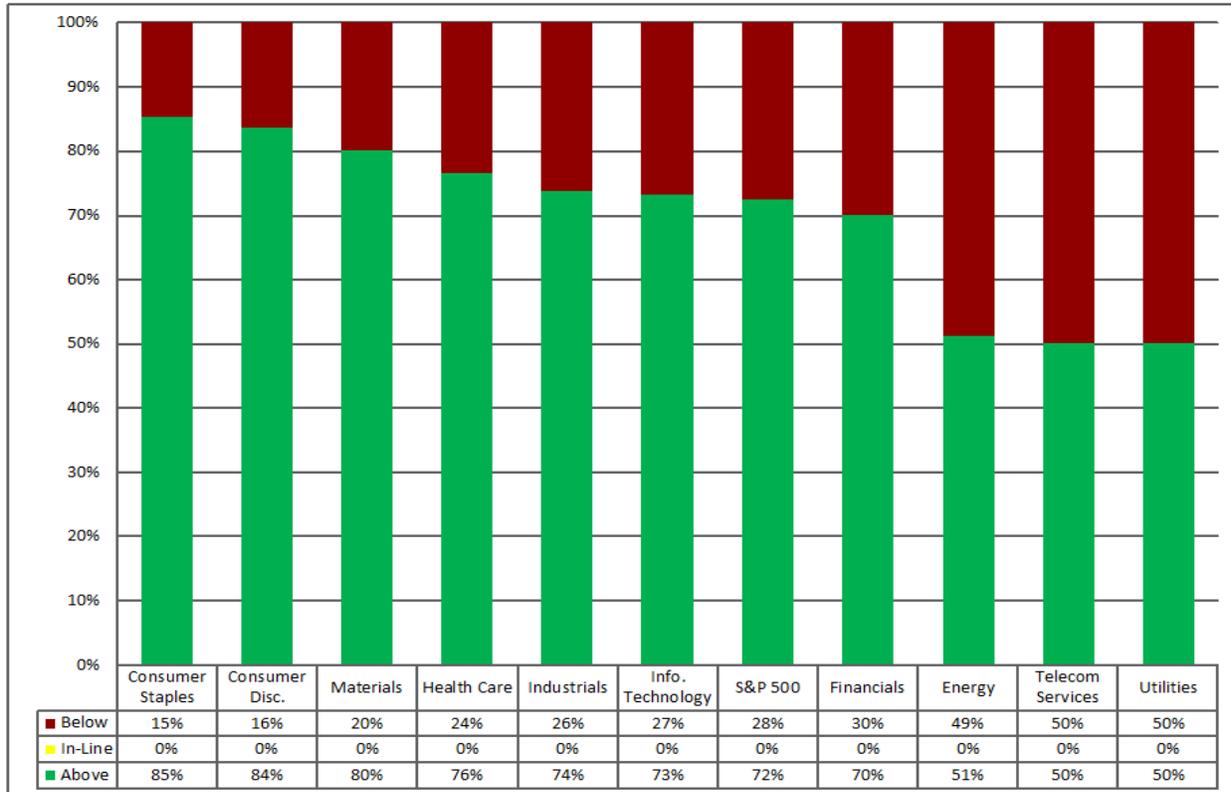
Will there be a return to the 10-year average valuation for the market anytime soon? If there is going to be a return to this average P/E ratio of 14.4, either future estimates will need to decrease, the price of the index will need to increase, or a combination of the two will need to occur.

**Companies Reporting Next Week**

During the next couple of weeks, the first few companies will report earnings for Q2 2012. During the upcoming week, no companies in the S&P 500 are scheduled to release results for Q2 2012.

Q1 2012: Scorecard

Q1 2012 Earnings: Above, In-Line, Below Estimates

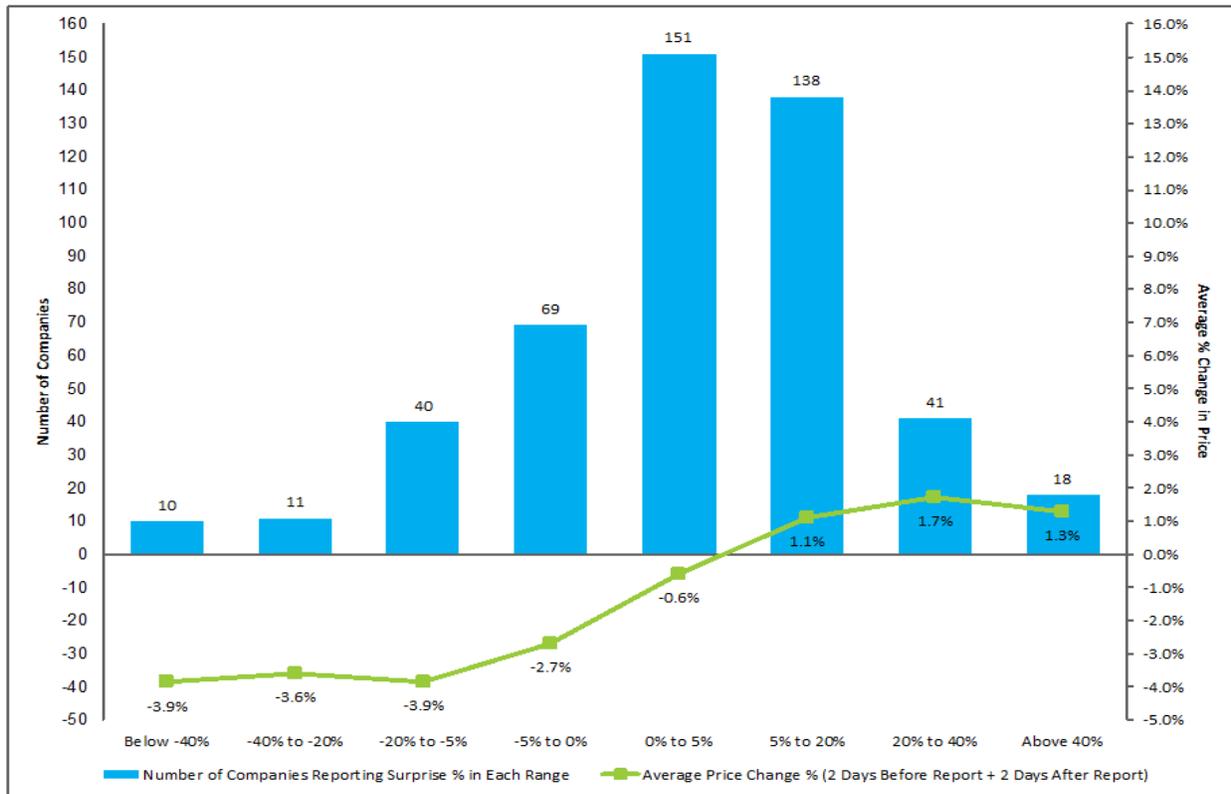


Q1 2012 Revenues: Above, In-Line, Below Estimates

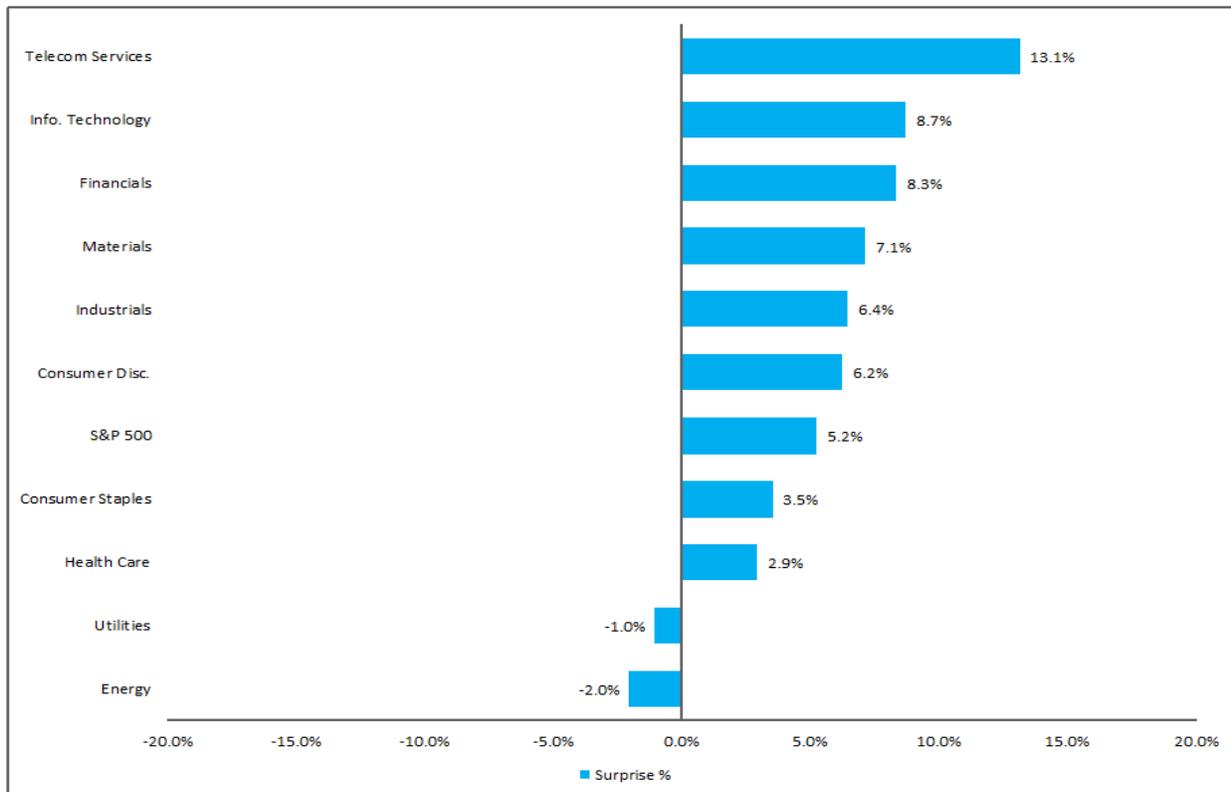


Q1 2012: Scorecard

Q1 2012: Surprise % vs. Average Price Change %

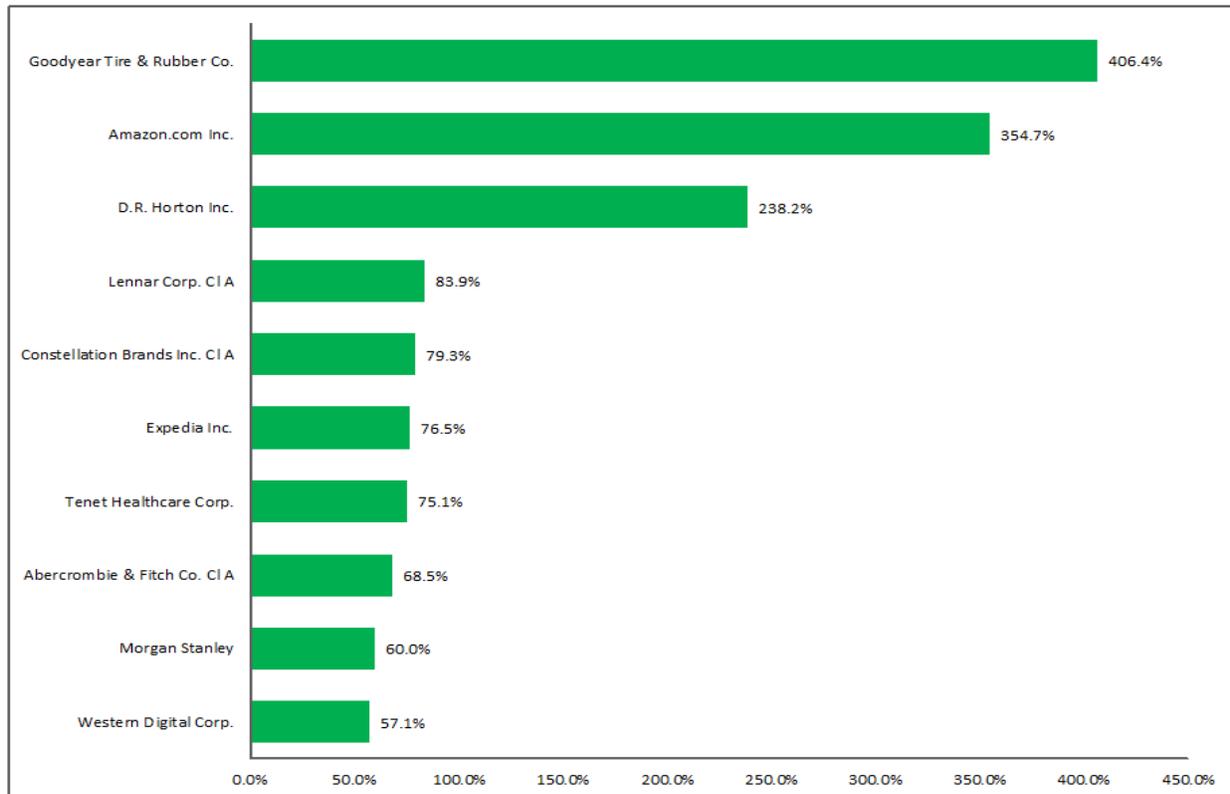


Q1 2012: Sector Level Surprise %

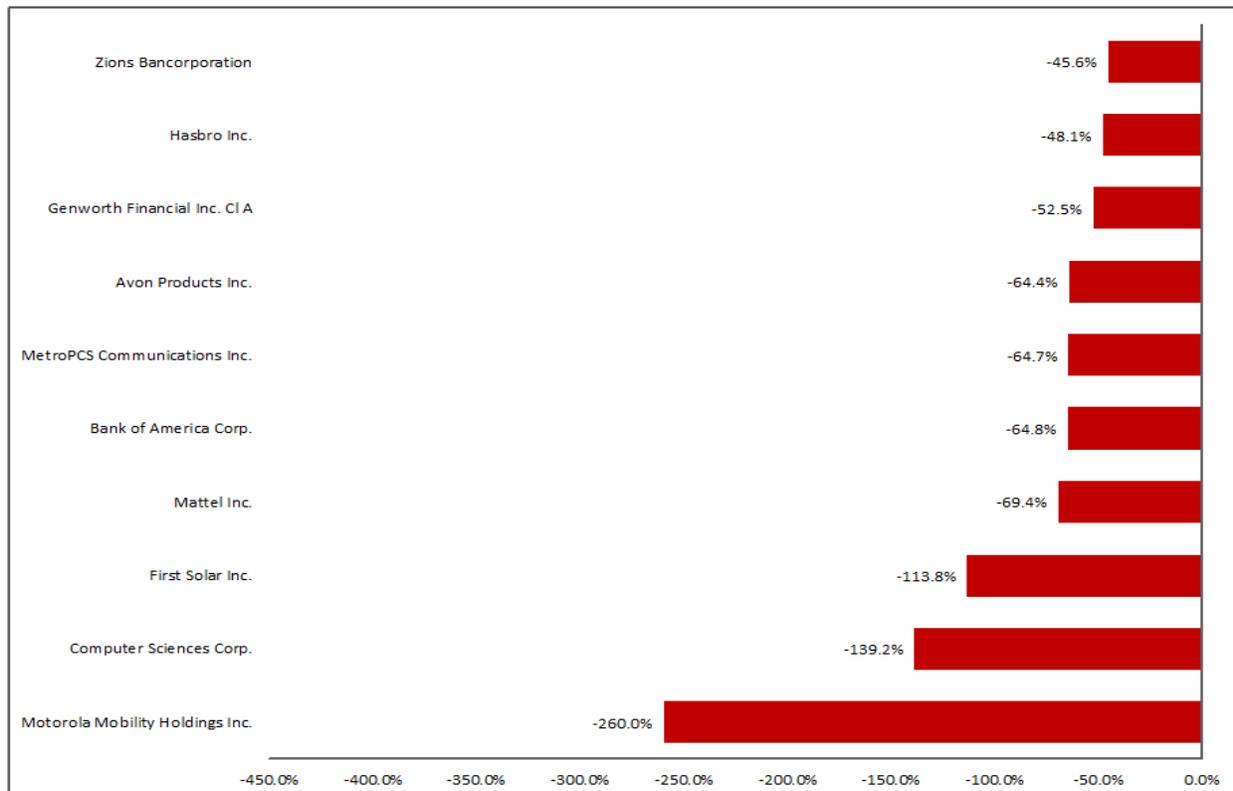


Q1 2012: Scorecard

Surprise %: Top 10 Companies



Surprise %: Bottom 10 Companies

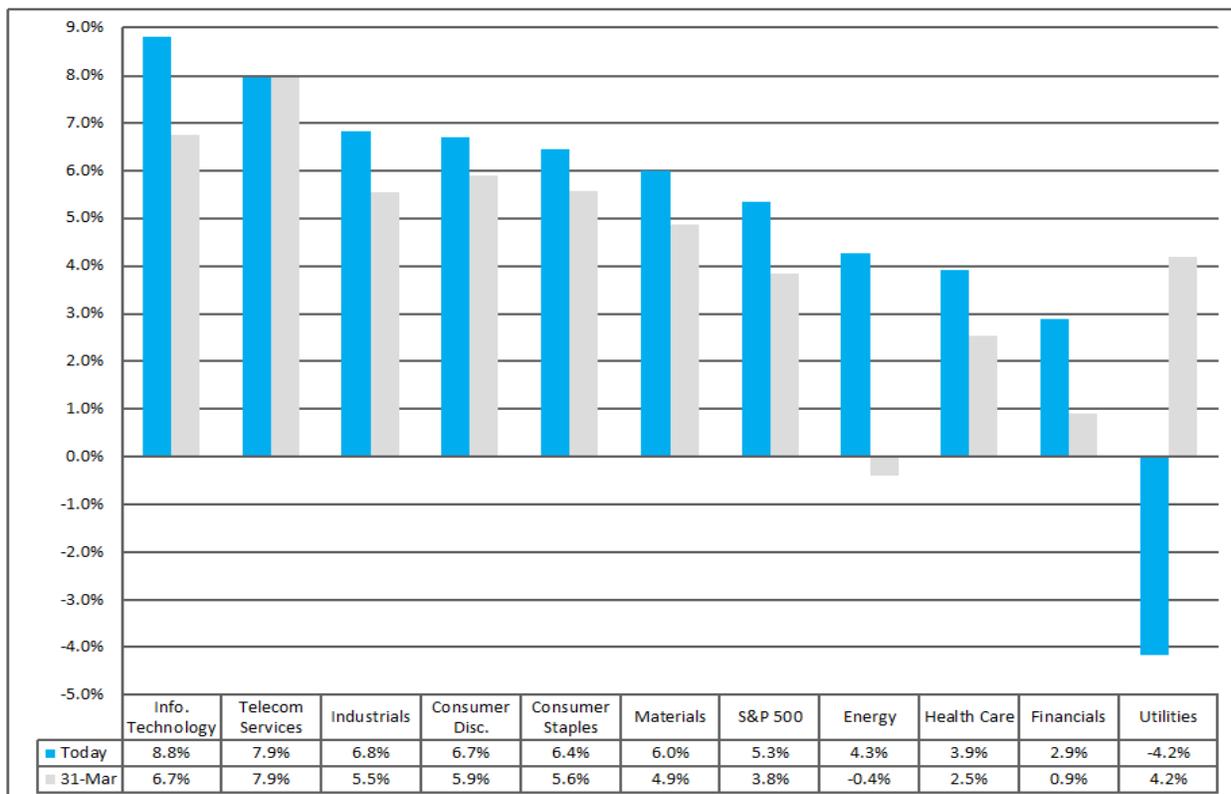


Q1 2012: Growth

Q1 2012 Earnings Growth

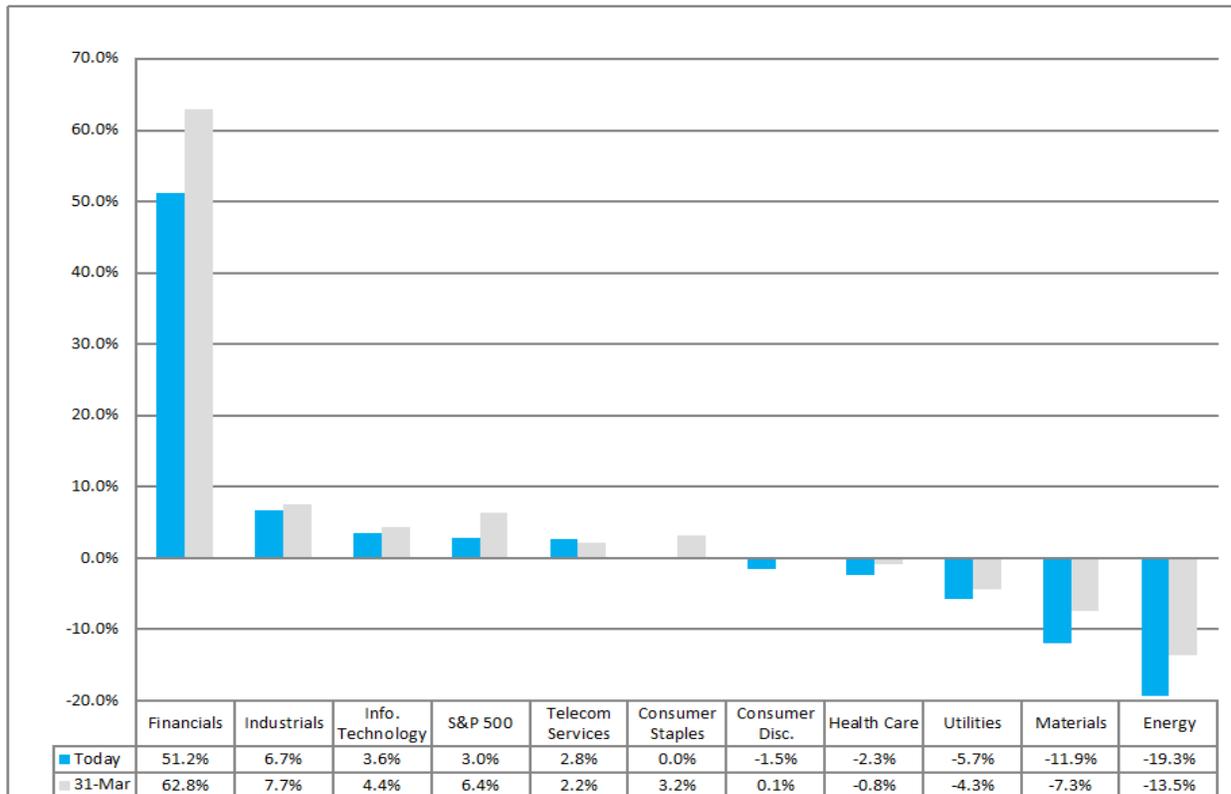


Q1 2012 Revenue Growth



Q2 2012: Growth

Q2 2012 Earnings Growth

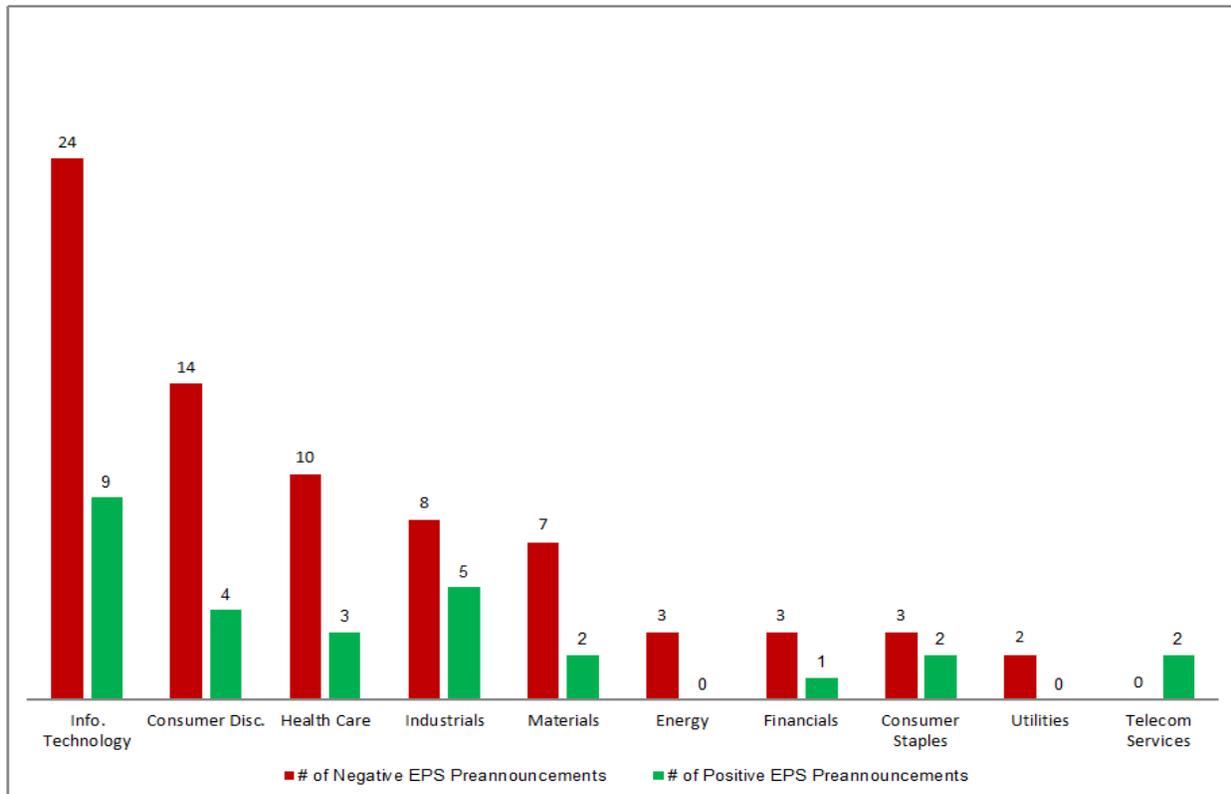


Q2 2012 Revenue Growth



## Guidance: Current Fiscal Quarter

Number of Positive & Negative EPS Preannouncements: Current Fiscal Quarter

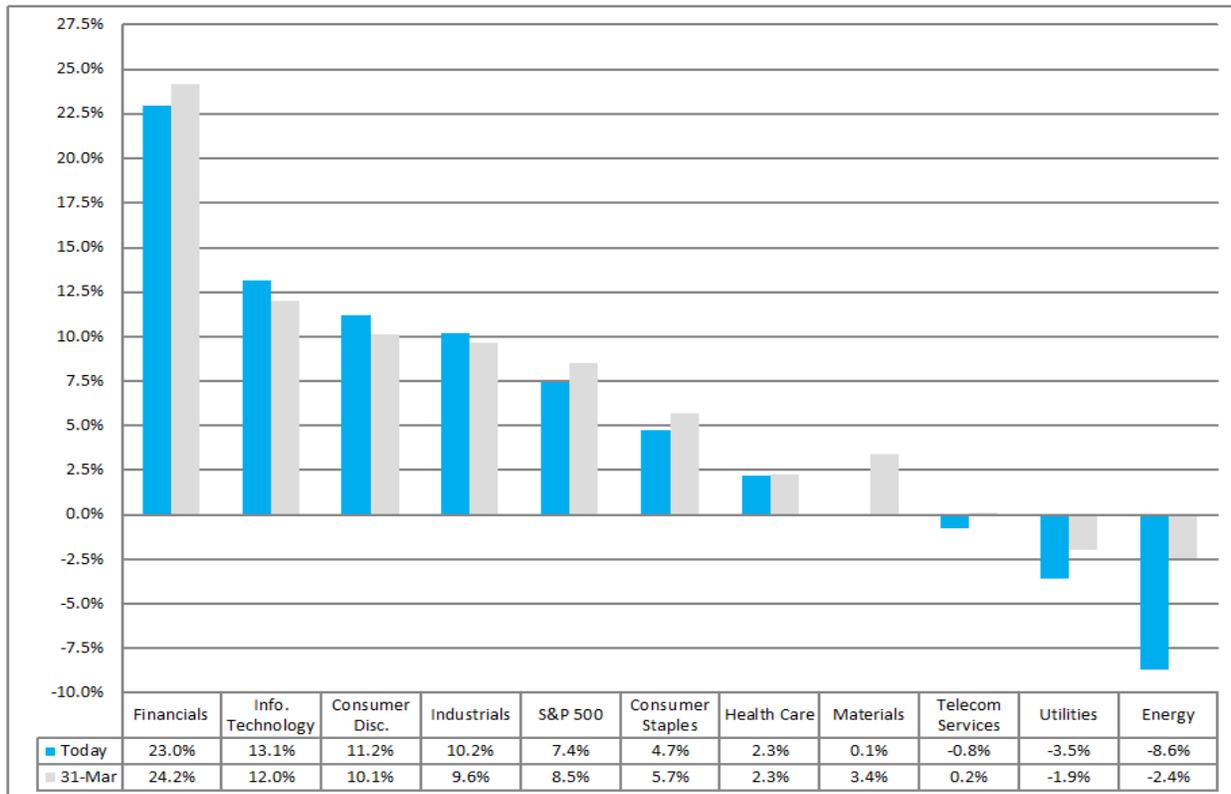


Percentage of Positive & Negative EPS Preannouncements: Current Fiscal Quarter

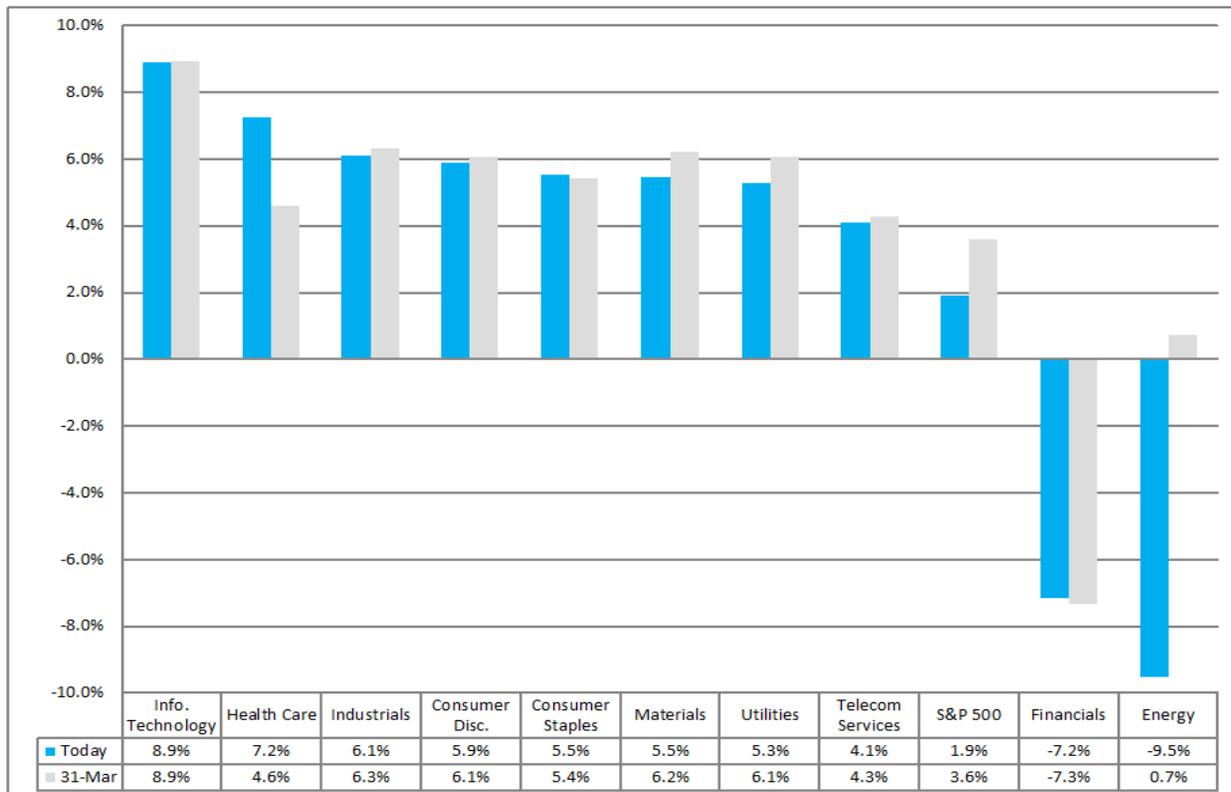


CY 2012: Growth

CY 2012 Earnings Growth

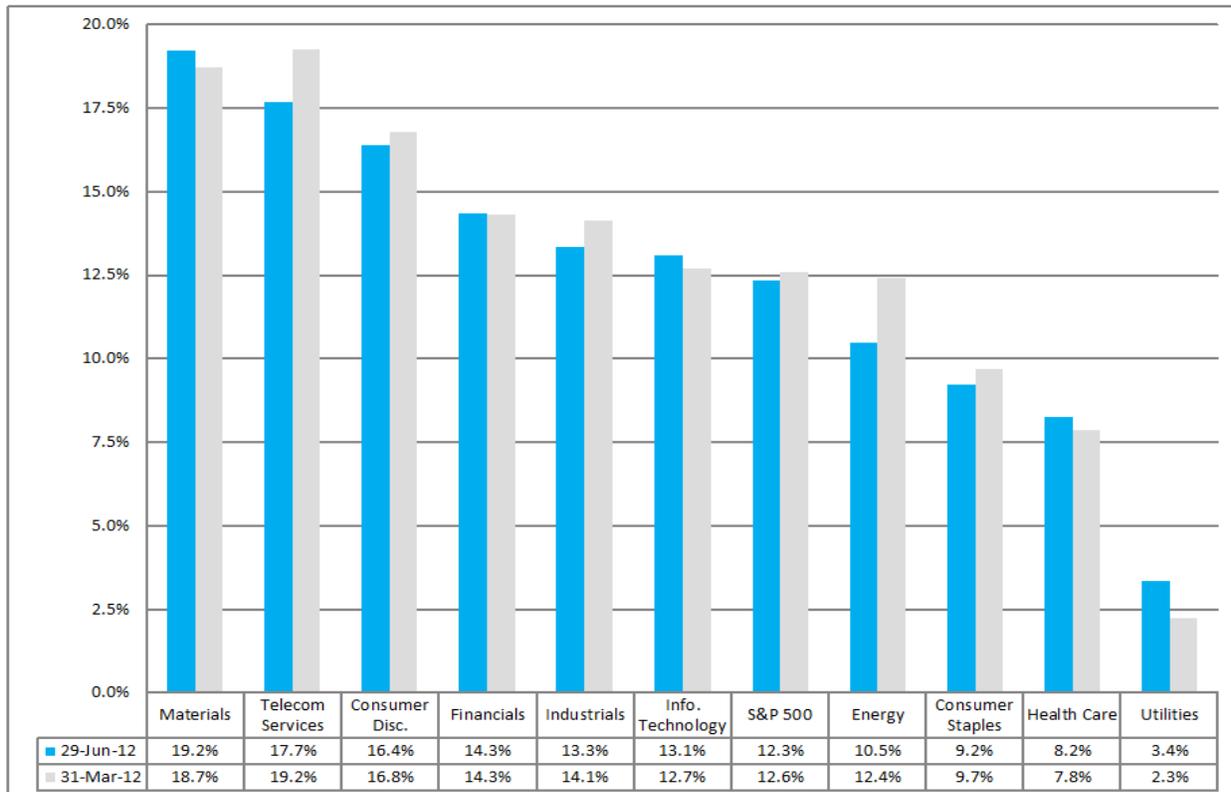


CY 2012 Revenue Growth

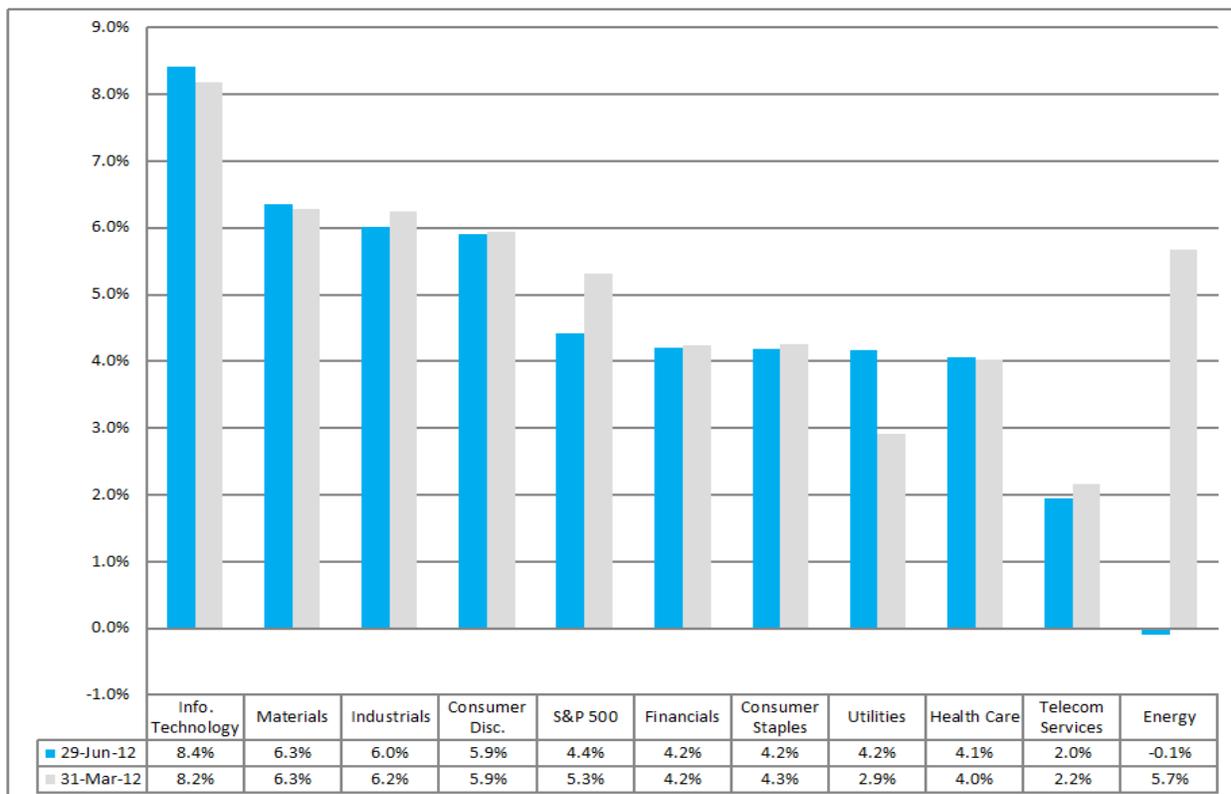


CY 2013: Growth

CY 2013 Earnings Growth

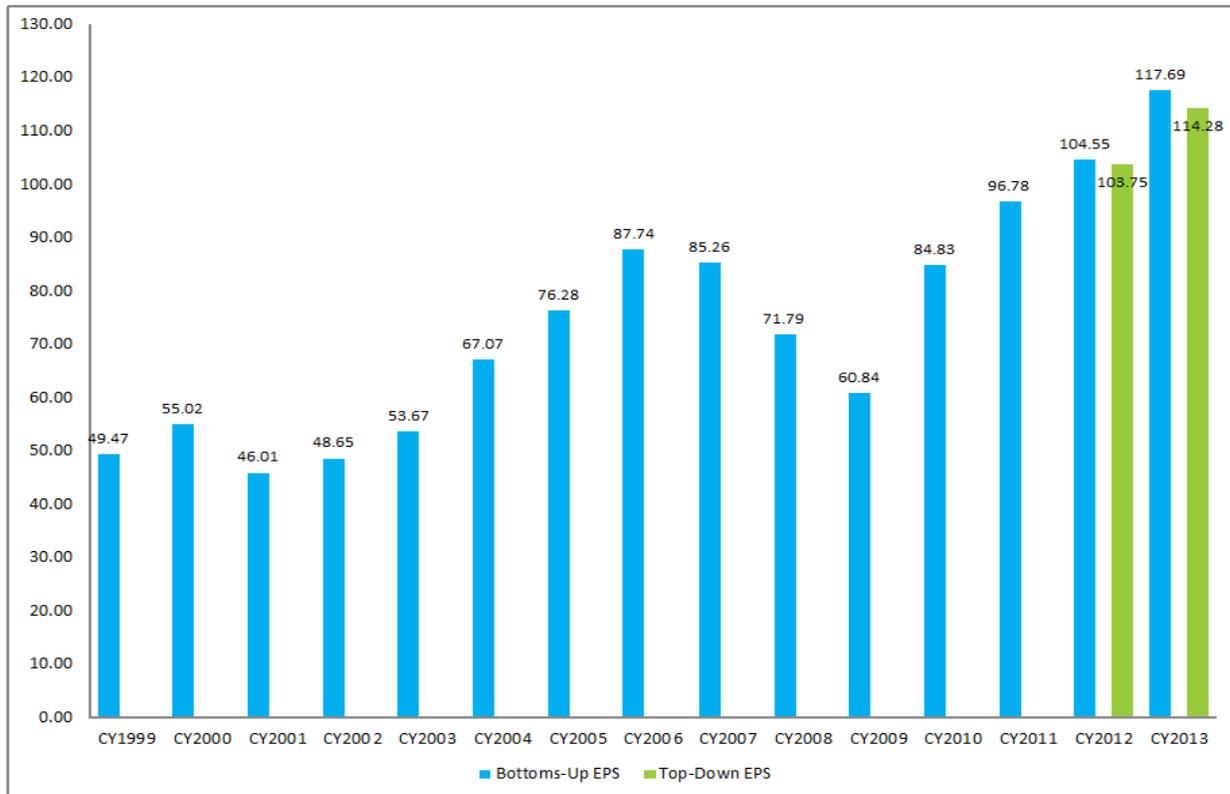


CY 2013 Revenue Growth

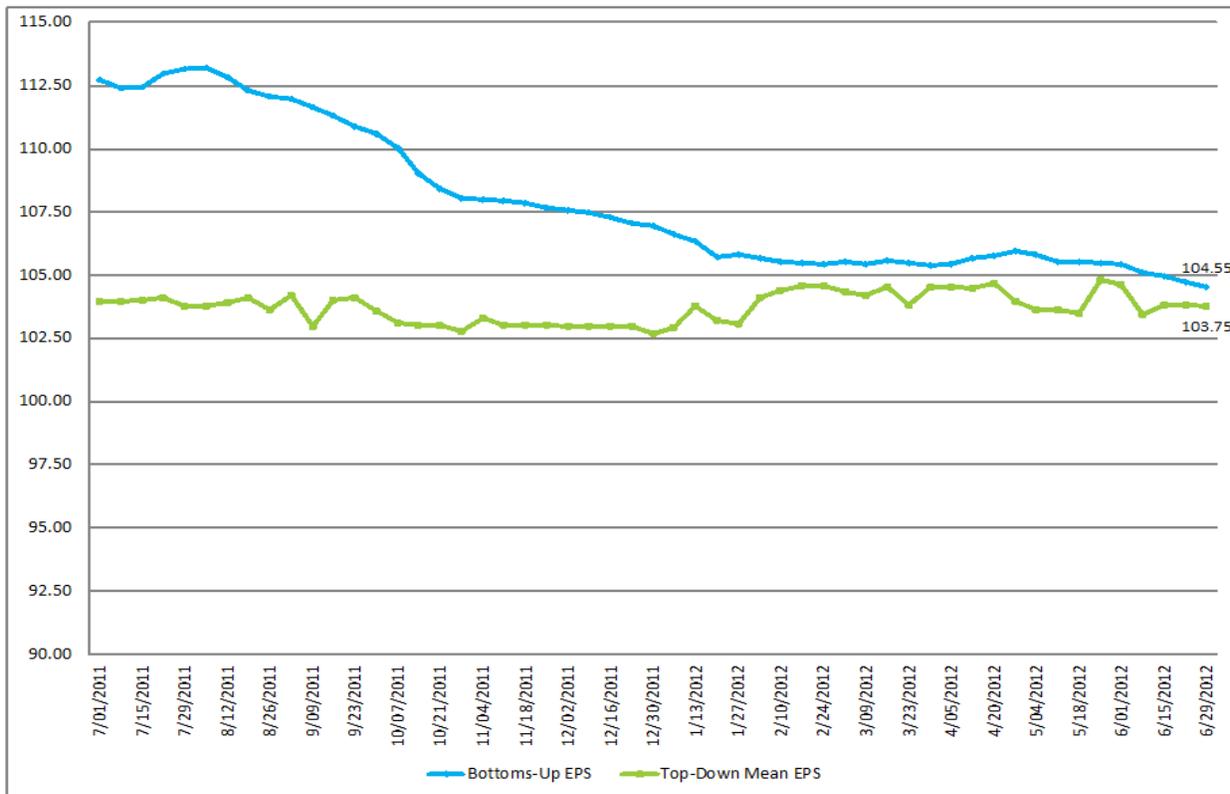


## Bottom-up Estimates

Calendar Year Bottom-Up EPS Actuals & Estimates

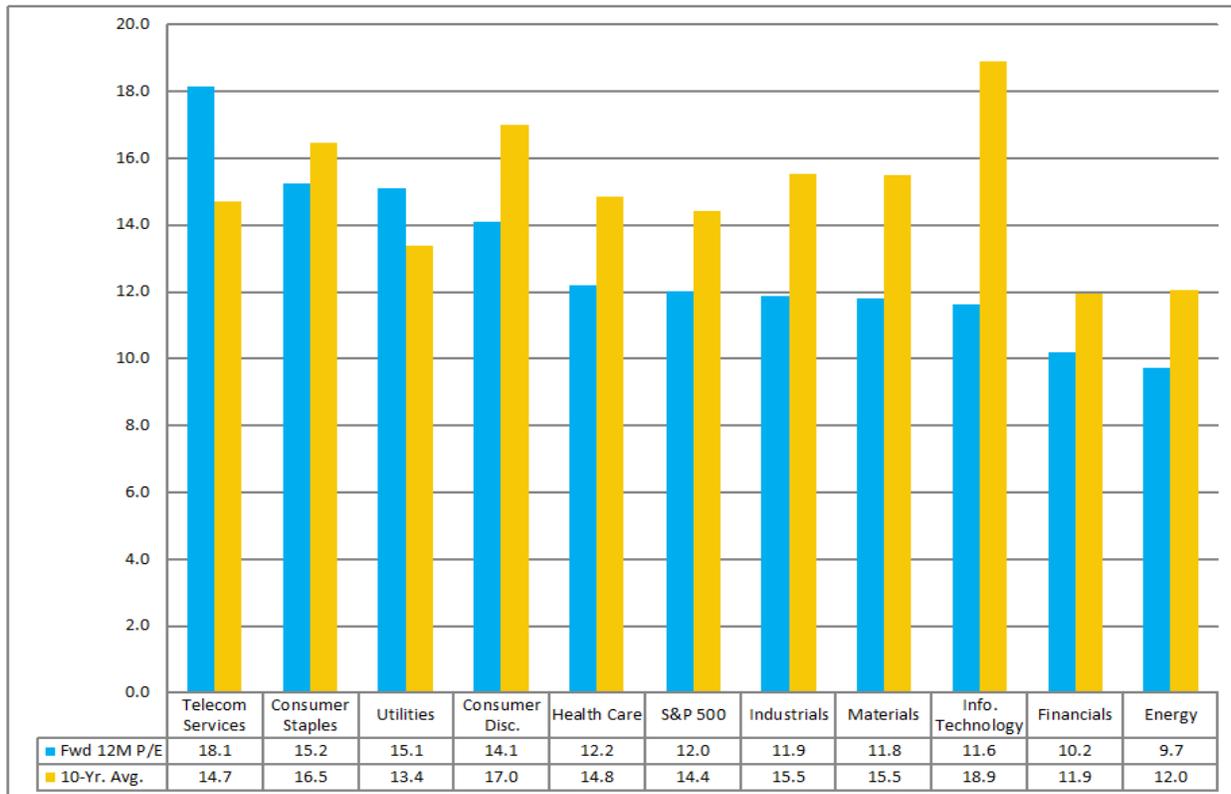


CY 2012 Estimates: Bottom-Up EPS vs. Top Down EPS

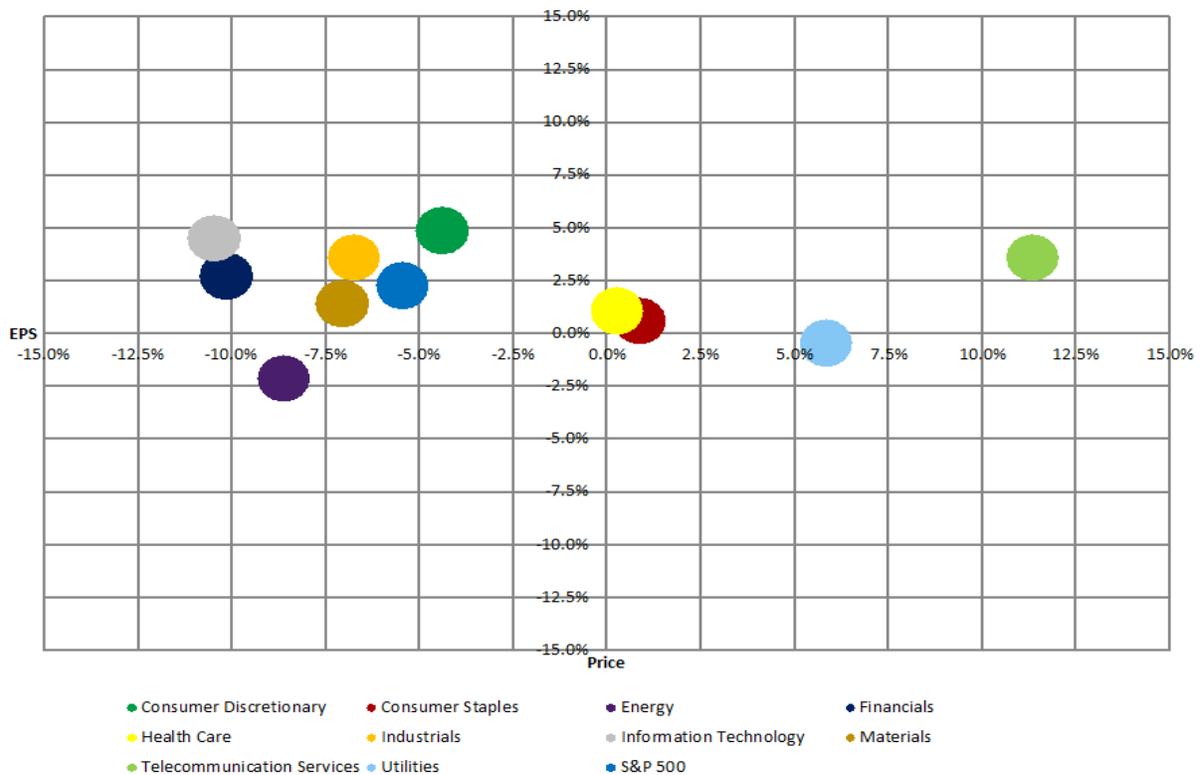


## Price / Earnings Ratio: Sector Level

Sector-Level Forward 12-Month P/E Ratios

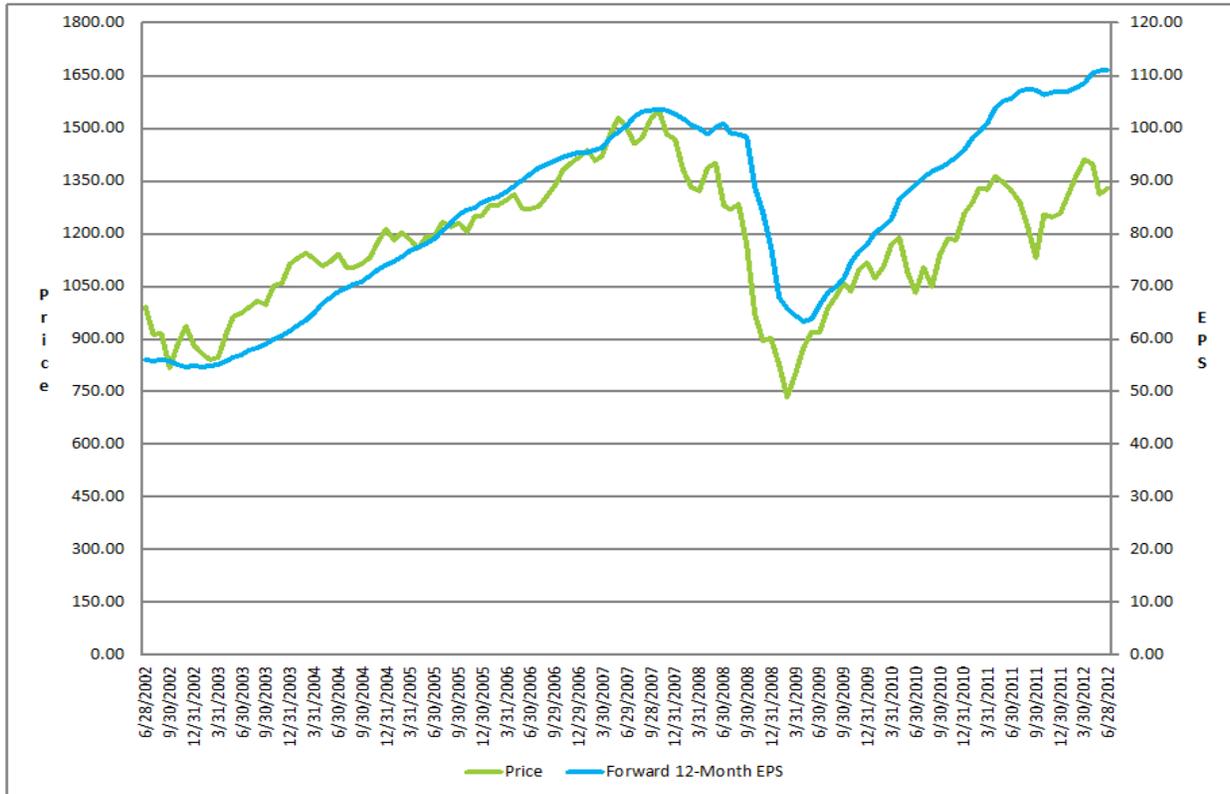


Sector-Level Change in Price vs. Change Forward 12M EPS: 3-Months

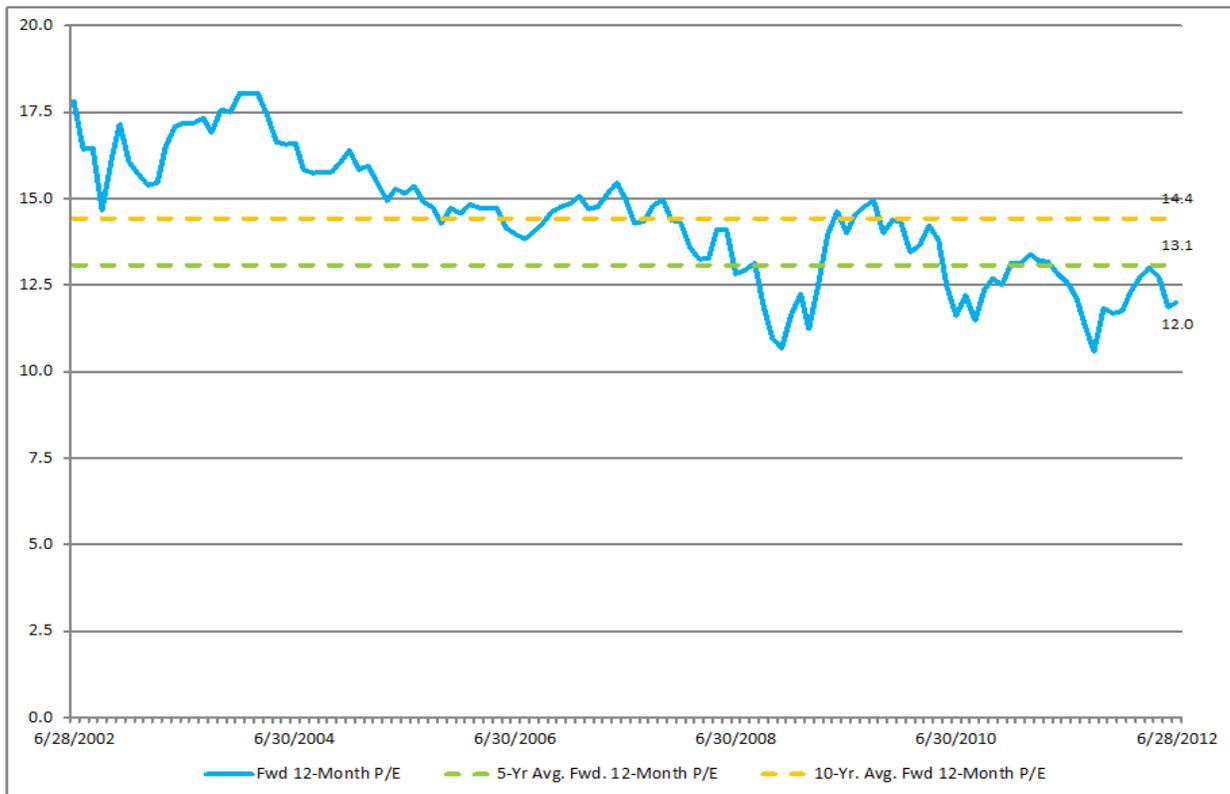


## Price / Earnings Ratio: Long-Term Averages

Change in Price vs. Change in Forward 12M EPS: 10-Year



Forward 12M P/E Ratio: 10-Years



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