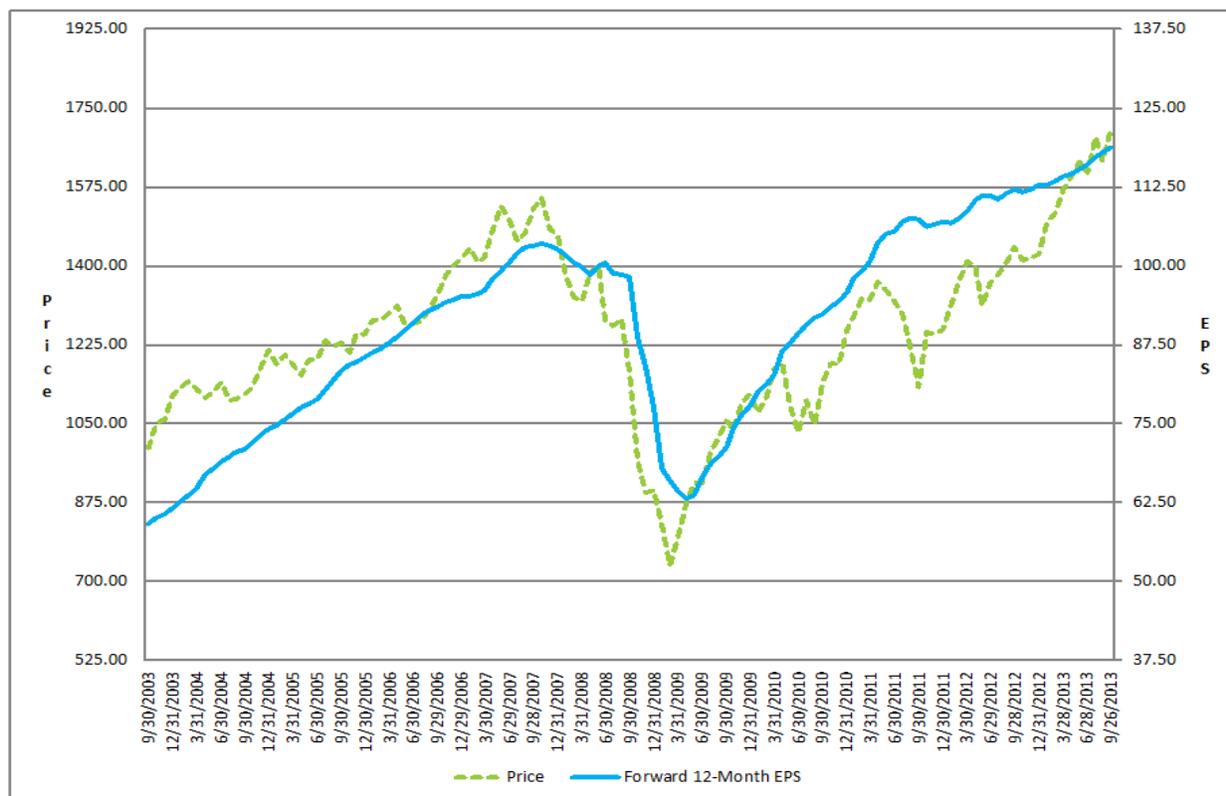


### Key Metrics

- + **Earnings Growth:** The estimated earnings growth rate for Q3 2013 is 3.2%. The Financials sector is predicted to report the highest earnings growth for the quarter, while the Health Care sector is predicted to report the lowest earnings growth for the quarter.
- + **Earnings Revisions:** On June 30, the earnings growth rate for Q3 2013 was 6.5%. All ten sectors have recorded a decline in expected earnings growth over this time frame, led by the Materials sector.
- + **Earnings Guidance:** For Q3 2013, 89 companies have issued negative EPS guidance and 19 companies have issued positive EPS guidance.
- + **Valuation:** The current 12-month forward P/E ratio is 14.4. This P/E ratio is above the 5-year (12.9) and 10-year (14.0) averages.
- + **Earnings Scorecard:** Of the 17 companies that have reported earnings to date for Q3 2013, 12 have reported earnings above the mean estimate and 11 have reported revenue 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

### Lower Estimate Cuts than Average for the S&P 500 for the Third Quarter

Over the course of the third quarter, analysts have lowered earnings estimates for companies in the S&P 500 for the quarter. The Q3 bottom-up EPS estimate (which is an aggregation of the estimates for all 500 companies in the index) has dropped 2.6% (to \$26.94 from \$27.65) since June 30. How significant is a 2.6% decline in the aggregate EPS estimate during the quarter? How does this decrease compare to recent quarters?

During the past year (4 quarters), the average decline in the EPS estimate during the quarter has been 4.4%. During the past five years (20 quarters), the average decline in the EPS estimate during the quarter has been 6.4%. During the past ten years, (40 quarters), the average decline in the EPS estimate during the quarter has been 4.2%. Thus, the decline in the EPS estimate recorded during the course of the Q3 2013 quarter was lower than the trailing 1-year, 5-year, and 10-year averages. In fact, the decline in the bottom-up EPS during the third quarter was the lowest since Q1 2011 (-0.7%)

Although the percentage reduction was lower than average, analysts did take down earnings estimates during the quarter. At the same time, the value of the S&P 500 increased 5.8% (to 1698.67 from 1606.28), and has closed near record high values in recent weeks. Is it unusual for the earnings estimate for the index to decline and the value of the index to increase during the course of a quarter?

In recent quarters, it has not been unusual for the value of the index to increase at the same time analysts are trimming earnings estimates for the same quarter. In fact, it has occurred in 12 of the past 20 quarters (including Q3 2013). During these 12 quarters, the average decrease in the bottom-up EPS has been 2.9%, while the average increase in the value of the index has been 8.6%.

S&P 500 Q3 2013: Change in EPS vs. Change in Price



## Q3 2013 Earnings Season: Overview

### Slight Drop in Earnings Growth This Week, But Has Been Cut in Half since June 30

#### No Change in Earnings Growth Rate This Week

The estimated earnings growth rate for the third quarter is 3.2% this week, slightly below the estimated growth rate of 3.3% last week. During the week, small downward revisions to estimates for companies in the Financials sector (including JPMorgan Chase, Citigroup, and Goldman Sachs) were partially offset by the upside earnings surprises reported by companies in the Consumer Discretionary sector (including NIKE and Carnival). As a result, the estimated earnings growth rate for the Financials sector dropped to 9.4% from 10.2% during the week, while the estimated earnings growth rate for the Consumer Discretionary sector improved to 6.7% from 6.1% over this time frame.

#### Materials Sector Has Seen Largest Cuts to Earnings Estimates Overall since June 30

The estimated earnings growth rate for Q3 2013 of 3.2% is also below the estimate of 6.5% at the start of the quarter (June 30). All ten sectors have recorded a decline in expected earnings growth during this time frame. The Materials sector has witnessed the largest decrease in predicted earnings growth since June 30, followed by the Energy, Consumer Staples, Information Technology, and Consumer Discretionary sectors.

The Materials sector has seen the largest drop in expected earnings growth (to 2.0% from 15.0%) since the start of the quarter. Companies in the Metals & Mining industry have witnessed the largest cuts to estimates during this time, including U.S. Steel (to -\$0.44 from -\$0.18), Allegheny Technologies (to \$0.01 from \$0.29), Newmont Mining (to \$0.32 from \$0.60), and Alcoa (to \$0.06 from \$0.10).

The Energy sector has recorded the second largest decrease in expected earnings growth (to -1.0% from 3.3%) since the beginning of the quarter. Companies that have seen significant reductions in EPS estimates include CONSOL Energy (to \$0.08 from \$0.21), Marathon Petroleum (to \$1.30 from \$2.92), Tesoro (to \$1.11 from \$2.17), Phillips 66 (to \$1.48 from \$2.14), and Valero Energy (to \$1.08 from \$1.52).

The Consumer Staples sector has seen the third largest drop in expected earnings growth (to 3.1% from 7.3%) since the start of the quarter. Companies that have recorded substantial cuts to estimates during this time include Safeway (to \$0.16 from \$0.45), Avon Products (to \$0.19 from \$0.25), Archer-Daniels-Midland Company (to \$0.46 from \$0.62), and Estee Lauder Companies (to \$0.73 from \$0.91).

The Information Technology sector has witnessed the fourth largest decrease in expected earnings growth (to 1.2% from 5.0%) since June 30. Companies that have recorded substantial reductions in EPS estimates include Intuit (to -\$0.09 from -\$0.02), Teradyne (to \$0.44 from \$0.60), KLA-Tencor (to \$0.66 from \$0.86), Autodesk (to \$0.39 from \$0.51), and Microsoft (to \$0.55 from \$0.68).

The Consumer Discretionary sector has recorded the fifth largest decline in expected earnings growth (to 6.7% from 10.4%) since the beginning of the quarter. Companies in retail industries have seen the largest cuts to estimates during this time, including Amazon.com (to -\$0.10 from \$0.07), J. C. Penney (to -\$1.67 from -\$0.75), Abercrombie & Fitch (to \$0.44 from \$1.08), and Target (to \$0.64 from \$0.91).

#### EPS Guidance: More than 80% Negative for Q3

At this point in time, 108 companies in the index have issued EPS guidance for the third quarter. Of these 108 companies, 89 have issued negative EPS guidance and 19 have issued positive EPS guidance. As a result, 82% (89 out of 108) of the companies that have issued EPS guidance for the third quarter have issued negative EPS guidance. This percentage is consistent with the percentage recorded in the previous quarter at this time (81%), but well above the 5-year average of 62%.

For more details on guidance, please see the next edition of our *Guidance Quarterly* report, which will be published on Monday (September 30).

**Estimated Earnings Growth: 3.2%**

The estimated earnings growth rate for Q3 2013 is 3.2%. Eight of the ten sectors are expected to report higher earnings relative to a year ago, led by the Financials and Consumer Discretionary sectors. On the other hand, the Health Care and Energy sectors are the only two sectors predicted to report a year-over-year decrease in earnings for the quarter.

**Financials: Bank of America and Morgan Stanley Lead Growth**

The Financials sector is projected to have the highest earnings growth rate (9.3%) of any sector for the third consecutive quarter. It is also expected to be the largest contributor to earnings growth for the entire index. If the Financials sector is excluded, the earnings growth rate for the S&P 500 falls to 1.9%.

Four of the eight industries in the sector are predicted to report earnings growth for the quarter, led by the Capital Markets (58%) industry. Four of the eight industries are expected to report a year-over-year decline in earnings, led by the Thrift & Mortgage Finance (-11%) industry.

At the company level, Bank of America and Morgan Stanley are the key drivers of growth in the sector, due in part to comparisons to weak earnings in the third quarter of 2012. The mean EPS estimate for Bank of America is \$0.20, relative to year-ago EPS of \$0.00. The mean EPS estimate for Morgan Stanley is \$0.44, compared to year-ago EPS of -\$0.55. If both of these companies are excluded, the growth rate for the sector would fall to -0.4%.

**Consumer Discretionary: Broad-Based Growth across Sector**

The Consumer Discretionary sector is expected to have the second highest earnings growth rate at 6.7%. Growth is predicted to be broad-based across the sector. Nine of the twelve industries in the sector are projected to see earnings growth, led by the Internet & Catalog Retail (81%), Household Durables (17%), and Auto Components (16%) industries. At the other end of the spectrum, the Multiline Retail (-22%) and Automobiles (-7%) industries are expected to have the lowest earnings growth rates for the quarter.

**Health Care: Lowest Growth Expected**

The Health Care sector is predicted to have the lowest earnings growth rate of all ten sectors at -1.5%. Four of the six industries in the sector are expected to report a year-over-year decrease in earnings, led by the Health Care Equipment & Supplies (-4%) and Pharmaceuticals (-2%) industries.

**Energy: Chevron vs. Exxon Mobil**

The Energy sector is expected to have the second lowest earnings growth of any sector at -1.0%. However, only two of the seven sub-industries in this sector are expected to report a decline in earnings: Coal & Consumable Fuels (-92%) and Oil & Gas Refining & Marketing (-52%). On the other end of the spectrum, the Oil & Gas Storage & Transportation (50%) and Oil & Gas Exploration & Production (21%) sub-industries have the highest earnings growth rates.

At the company level, Chevron is the largest contributor to earnings growth for the sector, while Exxon Mobil is the largest detractor to earnings growth. The mean EPS estimate for Chevron is \$3.10, relative to year-ago actual EPS of \$2.38. If Chevron is excluded, the growth rate for the sector would drop to -6.3%. On the other hand, the mean EPS estimate for Exxon Mobil is \$1.93, compared to year-ago EPS of \$2.09. If Exxon Mobil is excluded, the growth rate for the Energy sector would improve to 4.1%.

**Estimated Revenue Growth: 2.6%**

The estimated revenue growth rate for Q3 2013 is 2.6%, below the growth rate of 3.0% estimated at the end of the second quarter (June 30). Nine of the ten sectors are predicted to report revenue growth for the quarter, led by the Utilities and Consumer Discretionary sectors. The Energy sector is the only sector expected to report a year-over-year decline in sales in the quarter.

The Utilities sector is expected to report the highest revenue growth at 6.7%. While all four industries are predicted to report growth, the Independent Power Producers & Energy Traders (34%) and Gas Utilities (17%) industries have the highest expected sales growth rates in the sector.

The Consumer Discretionary sector has the second highest revenue growth rate at 5.3%. Growth is predicted to be broad-based across the sector. At the industry level, eleven of the twelve industries in the sector are expected to report earnings growth, led by the Internet & Catalog Retail (22%), Distributors (12%), and Household Durables (12%) industries.

The Energy sector has the lowest revenue growth rate of all ten sectors at -1.3%. At the sub-industry level, three of the seven sub-industries are predicted to report a decrease in revenues: Coal & Consumable Fuels (-7%), Integrated Oil & Gas (-5%), and Oil & Gas Refining & Marketing (-3%). At the company level, Hess Corporation and Exxon Mobil are the largest detractors to growth in the sector. The mean sales estimate for Hess Corporation is \$2.4 billion, compared to sales of \$9.6 billion in the year-ago quarter. The mean sales estimate for Exxon Mobil is \$110.0 billion, relative to sales of \$115.7 billion in the year-ago quarter. Excluding these two companies, the revenue growth rate for the Energy sector improves to 3.0%.

### Global Concerns: F/X Rates, Europe and Emerging Markets

#### Less Favorable F/X Rates

The U.S. dollar has strengthened relative to the Japanese yen and other foreign currencies over the past year. In the year-ago quarter (Q3 2012), one dollar was equal to about \$78.62 yen on average. For Q3 2013 to date, one dollar has been equal to about \$98.92 yen on average. A number of companies commented on the negative impact of F/X rates on revenues and earnings for the second quarter. Will this trend continue in Q3?

*“For example, the year-over-year exchange rates for the yen for both the spot rate and the average rate have weakened 20% against the dollar. Other major FX moves occurred in India, Australia, Argentina and Brazil. These were somewhat offset by a slight strengthening of the euro. Overall, FX rates had a negative impact on our revenue and billings growth for the quarter although the impact on profitability was less pronounced.” –Red Hat (Sep. 23)*

*“I want to start by letting you know that currency in Q1 gave us a 2% headwind for new software license and total revenue which was more than my guidance last quarter.” –Oracle (Sep. 18)*

*“Year-over-year, FX rate changes had an \$18 million negative impact on reported revenue.” –Adobe Systems (Sep. 17)*

#### Europe

Europe has been reporting weak economic growth in recent quarters. According to FactSet Economics, the European Union recorded no growth in GDP (0.0%) in Q2 2013. A number of companies stated that economic conditions were still weak in Europe in the second quarter. However, some companies stated that conditions may have reached a bottom or improved slightly. Will companies see any improvement in Europe in the third quarter?

*“I think so from a macroeconomic situation, the one area that I called out was in particular the EMEA region had its lowest percentage of total bookings or total company bookings that they've had in some time. Having said that, I think their Q3 and Q4 is shaping up better and I'm hopeful that we're going to see some improvement there.” –Red Hat (Sep. 23)*

*“In Europe, first quarter sales in constant currency declined 3%, reflecting the tough operating environment in the region.” –General Mills (Sep. 18)*

### Emerging Markets

Economic growth for some countries in emerging markets regions has also been decreasing over the past year. According to FactSet Economics, two of the four “BRIC” countries recorded slower GDP growth in the most recent quarter. For Q2 2012, China and India recorded GDP growth of 7.6% and 3.4%, respectively. By Q2 2013, GDP growth rates for China and India had fallen to 7.5% and 2.4%.

On the other hand, Brazil has recorded an increase in GDP growth over the past year. For Q2 2013, Brazil reported GDP growth of 3.3%, above the 0.5% recorded in Q1 2012.

As a result, comments on business conditions in China and emerging markets continued to be mixed for Q2. Some companies reported weak conditions, while others saw strength. Will this trend continue in the third quarter?

*“And by the way, while many of you have commented on the softening in emerging market economies overall, I mean, I do want to point out that our business continues to be very strong in emerging markets. We had a very strong quarter in China and we're seeing terrific growth in Brazil.” –General Mills (Sep.18)*

### Earnings Growth Rebound Still Projected for Q413, But Little Revenue Growth

Although analysts have reduced earnings growth expectations for Q4 2013 (to 10.2% from 11.8%) since June 30, they still expect a significant improvement in earnings growth in the fourth quarter of 2013 relative to recent quarters. For Q4 2013, five of the ten sectors are predicted to see double-digit earnings growth: Financials (26.9%), Industrials (18.2%), Materials (15.0%), Telecom Services (14.7%), and Consumer Discretionary (12.0%).

The estimated revenue growth rate for Q4 2013 of 0.9% is expected to be well below estimated earnings growth rate. The Financials sector accounts for much of this gap between expected earnings and revenue growth for the index, as the sector is projected to report the highest earnings growth of all ten sectors at 26.9%, but also the lowest revenue growth of all ten sectors at -9.3%. For more details on this dichotomy, please see our most recent *Market Insight* report titled, “Growth Divide in EPS & Sales in Q4,” which was published on September 25.

### Valuation: Forward P/E Ratio is 14.4, above the 10-Year Average (14.0)

The current forward 12-month P/E ratio for the index is 14.4. At the sector level, the Consumer Discretionary (17.4) and Consumer Staples (16.8) sectors have the highest forward 12-month P/E ratios, while the Financials (12.0) and Energy (12.4) sectors have the lowest forward 12-month P/E ratios.

The P/E ratio of 14.4 for the index as a whole is above the prior 5-year average forward 12-month P/E ratio of 12.9, and above the prior 10-year average forward 12-month P/E ratio of 14.0.

It is also above the forward 12-month P/E ratio of 14.1 recorded one month ago. During the past month, the price of the index increased by 2.5%, while the forward 12-month EPS estimate increased by 0.7%.

At the sector level, the Consumer Discretionary (to 17.4 from 16.8), Industrials (to 15.2 from 14.7), and Materials (to 15.6 from 15.1) sectors witnessed the largest increases in the forward 12-month P/E ratio over the past month. None of the ten sectors recorded a decrease in the forward 12-month P/E ratio during this time frame.

### Companies Reporting Next Week: 7

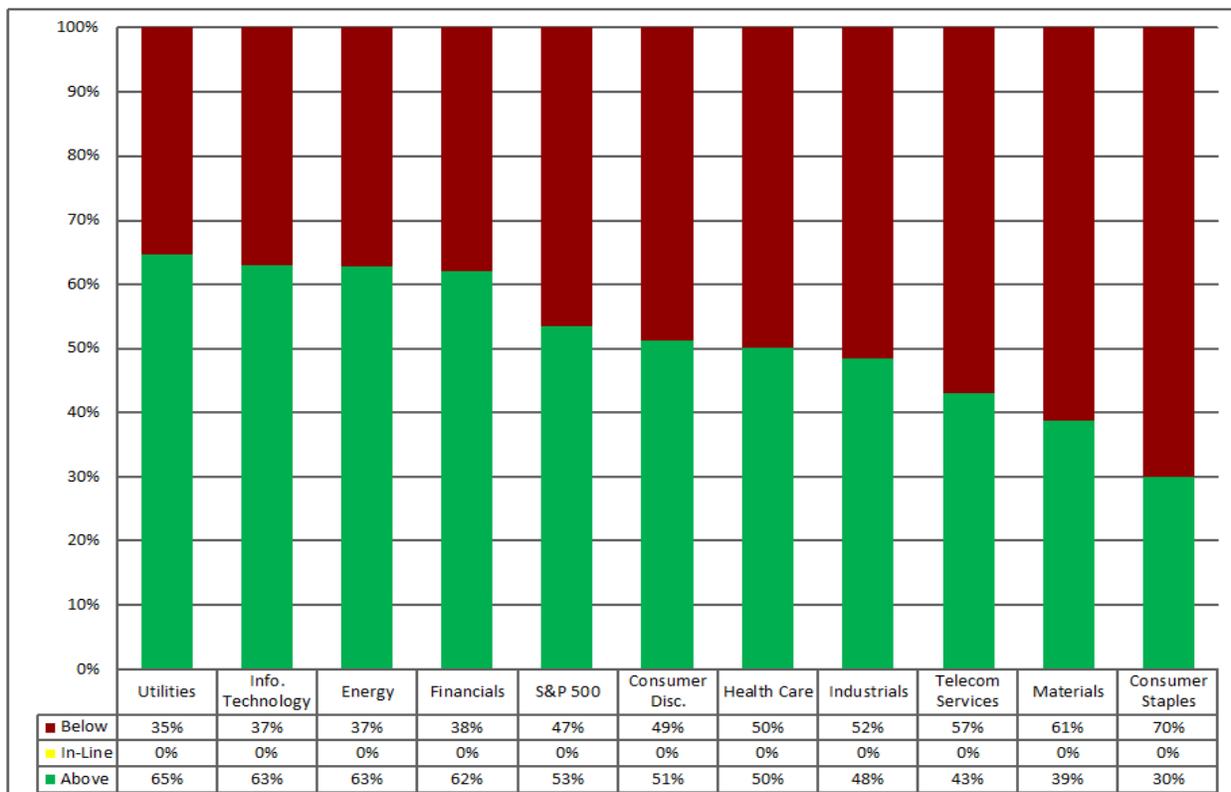
During the upcoming week, seven S&P 500 companies are scheduled to report earnings for the third quarter.

Q2 2013: Scorecard

Q2 2013 Earnings: Above, In-Line, Below Estimates

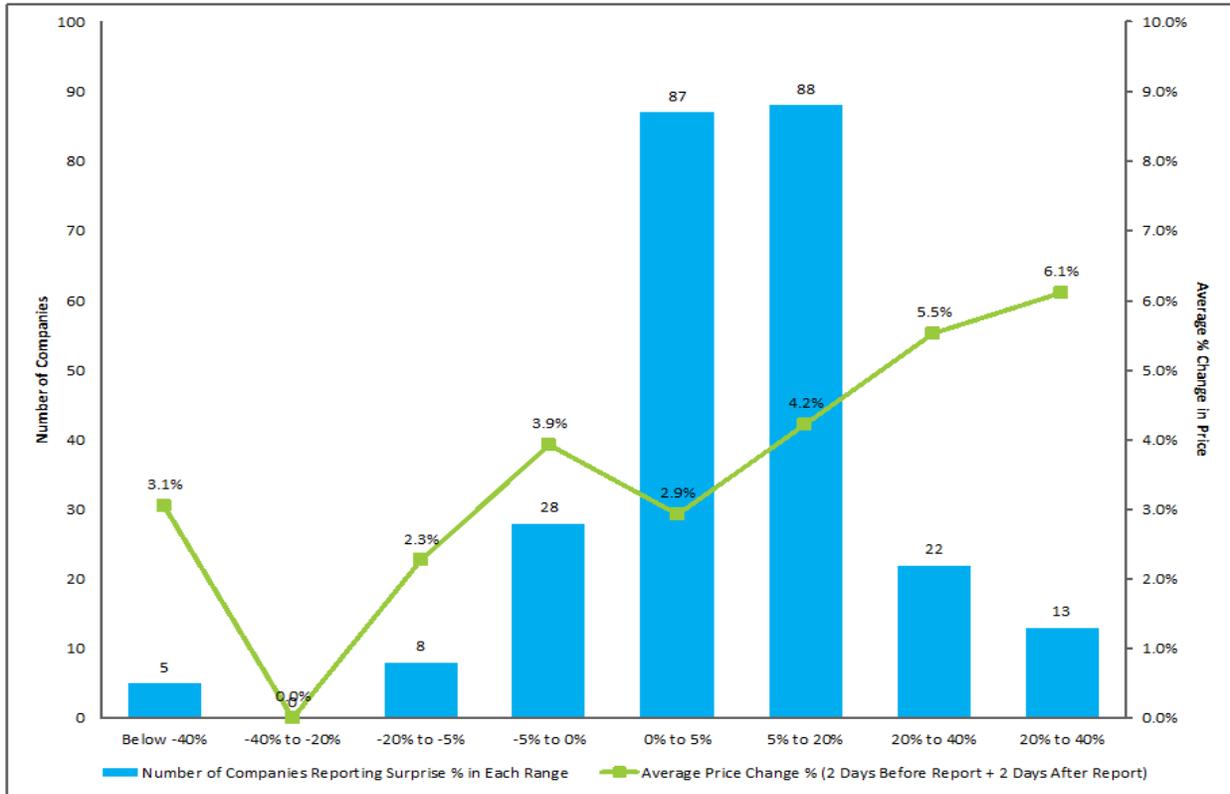


Q2 2013 Revenues: Above, In-Line, Below Estimates

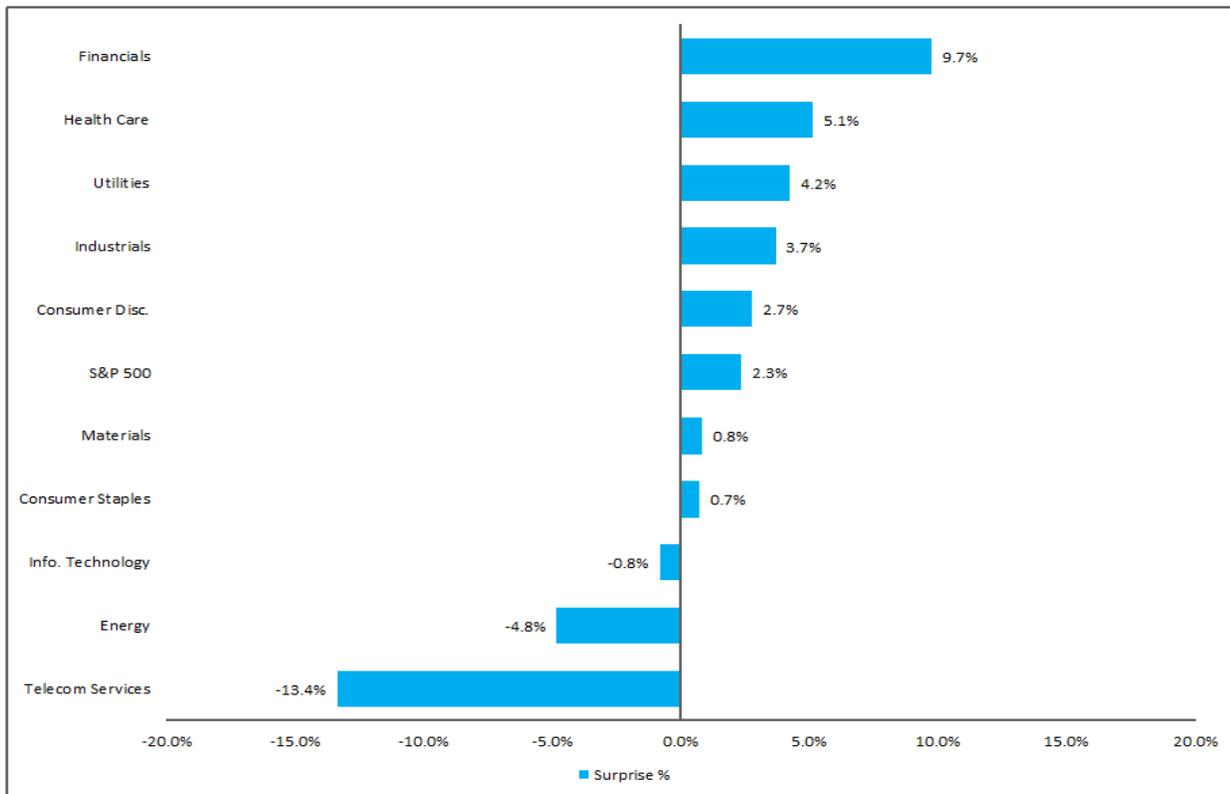


Q2 2013: Scorecard

Q2 2013: Surprise % vs. Average Price Change %

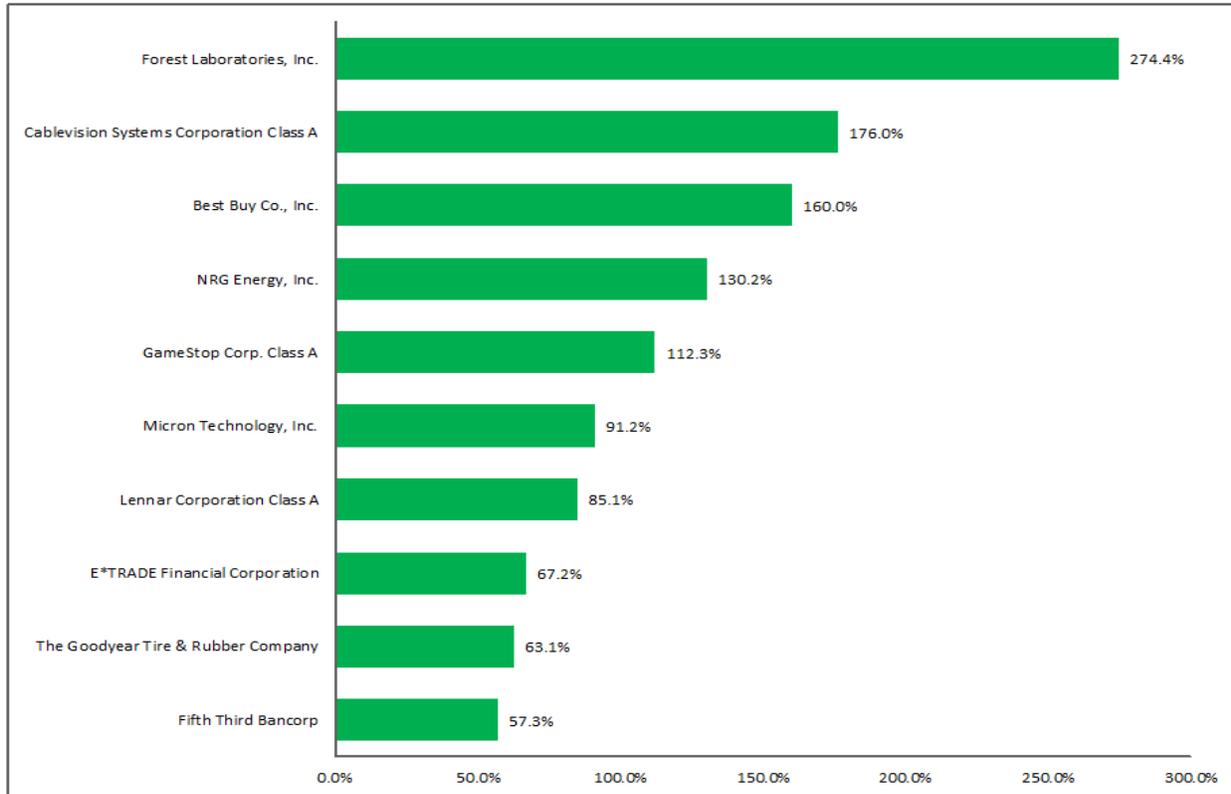


Q2 2013: Sector Level Surprise %

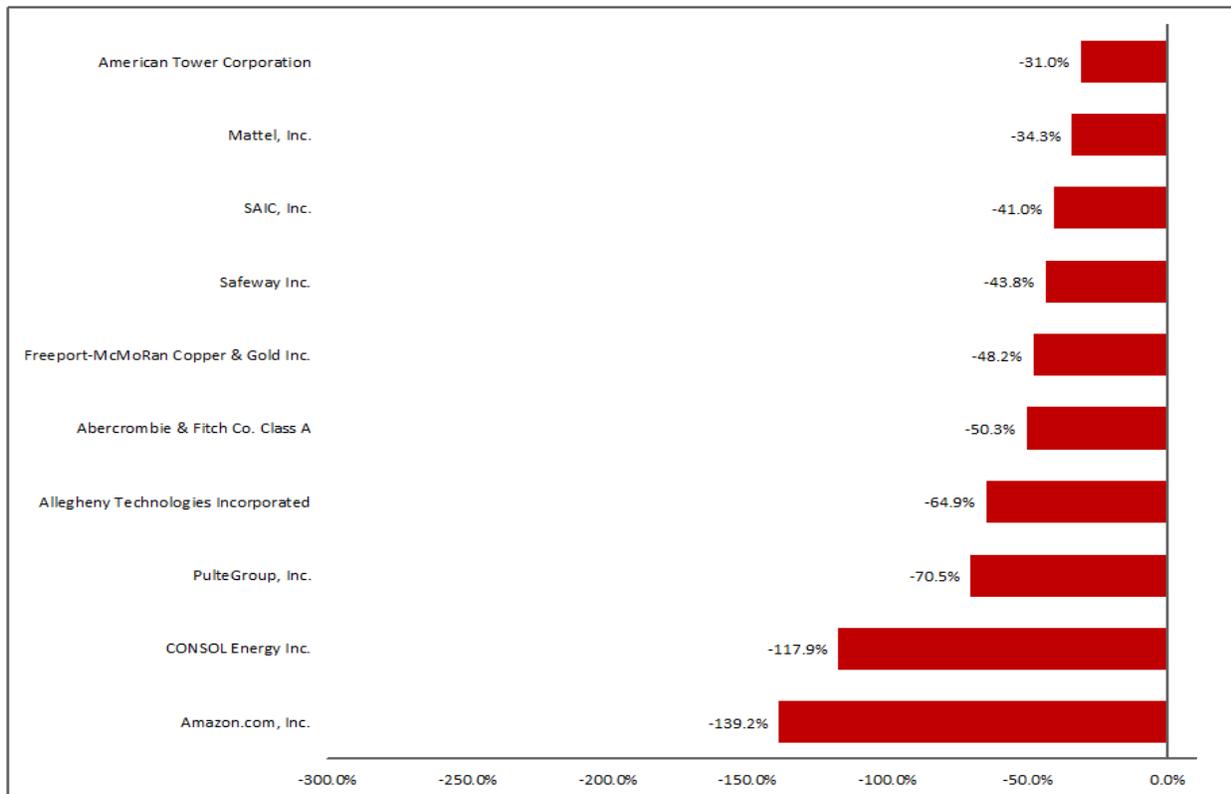


Q2 2013: Scorecard

EPS Surprise %: Top 10 Companies

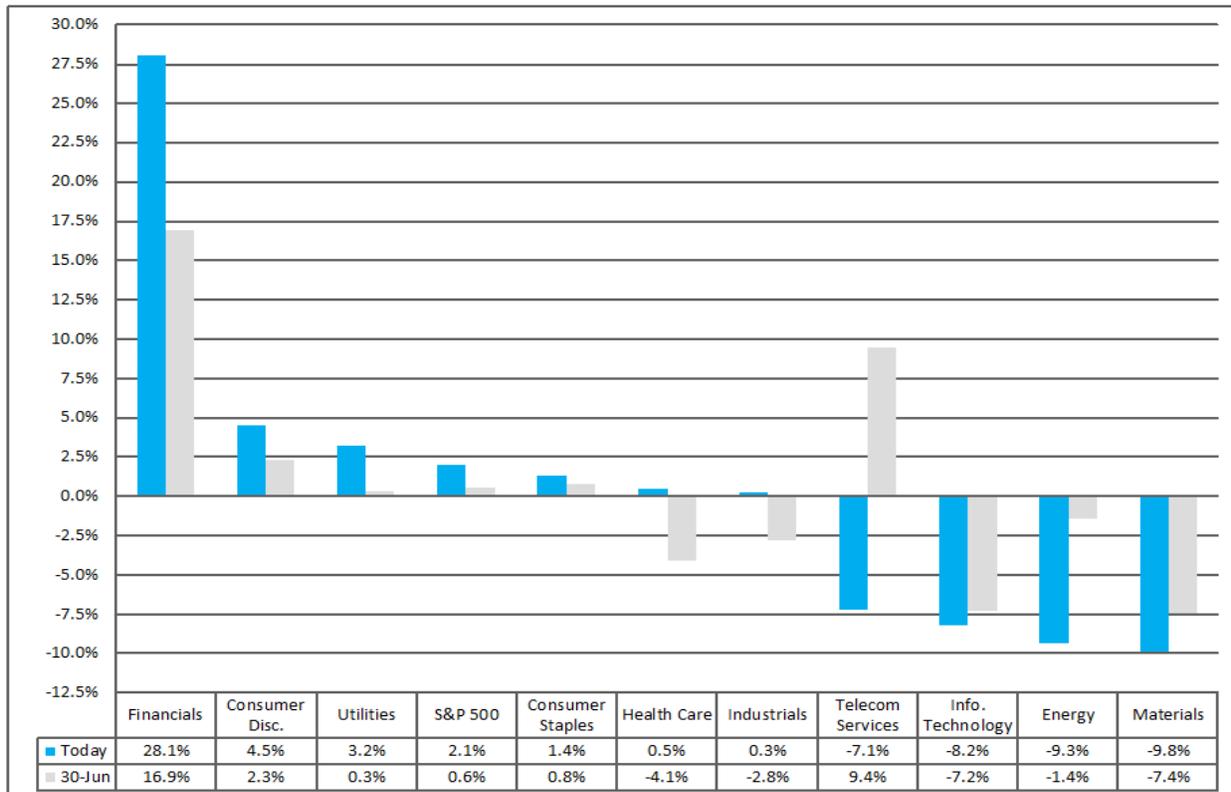


EPS Surprise %: Bottom 10 Companies

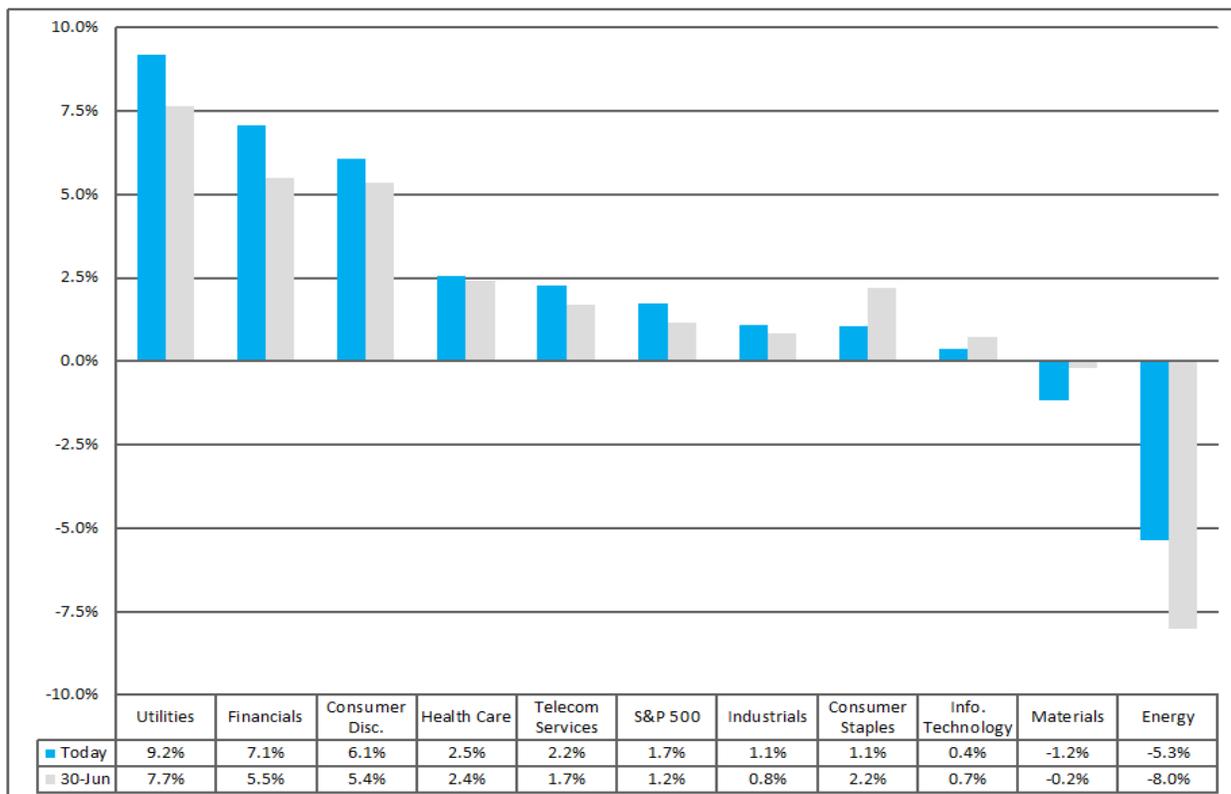


Q2 2013: Growth

Q2 2013 Earnings Growth

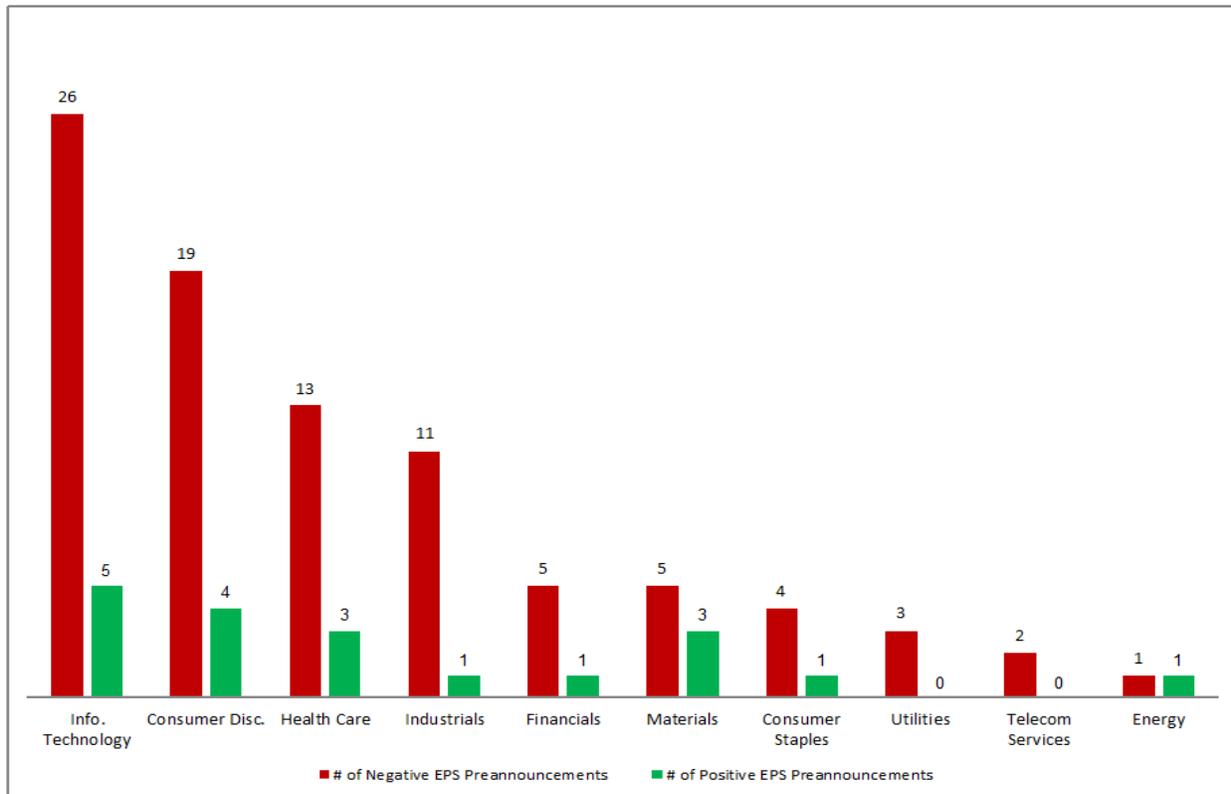


Q2 2013 Revenue Growth

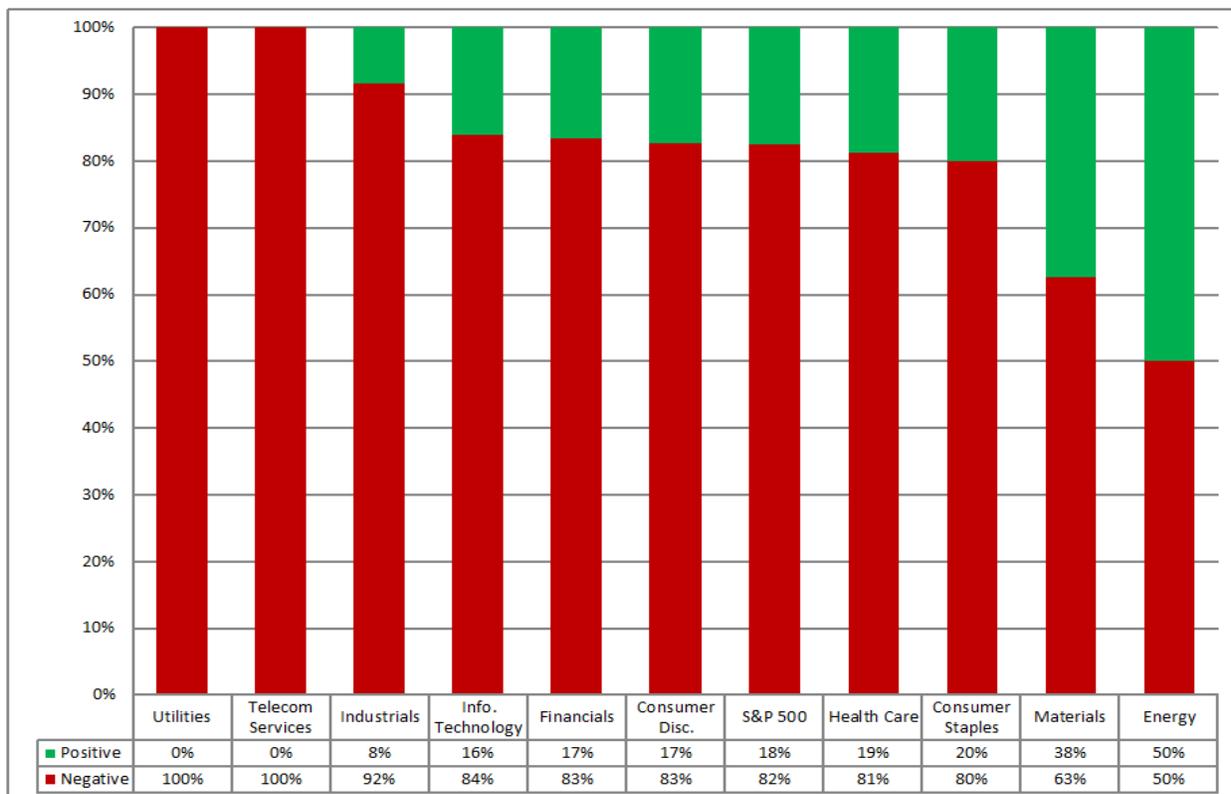


### Q3 2013: Guidance

Number of Positive & Negative EPS Preannouncements: Q3 2013

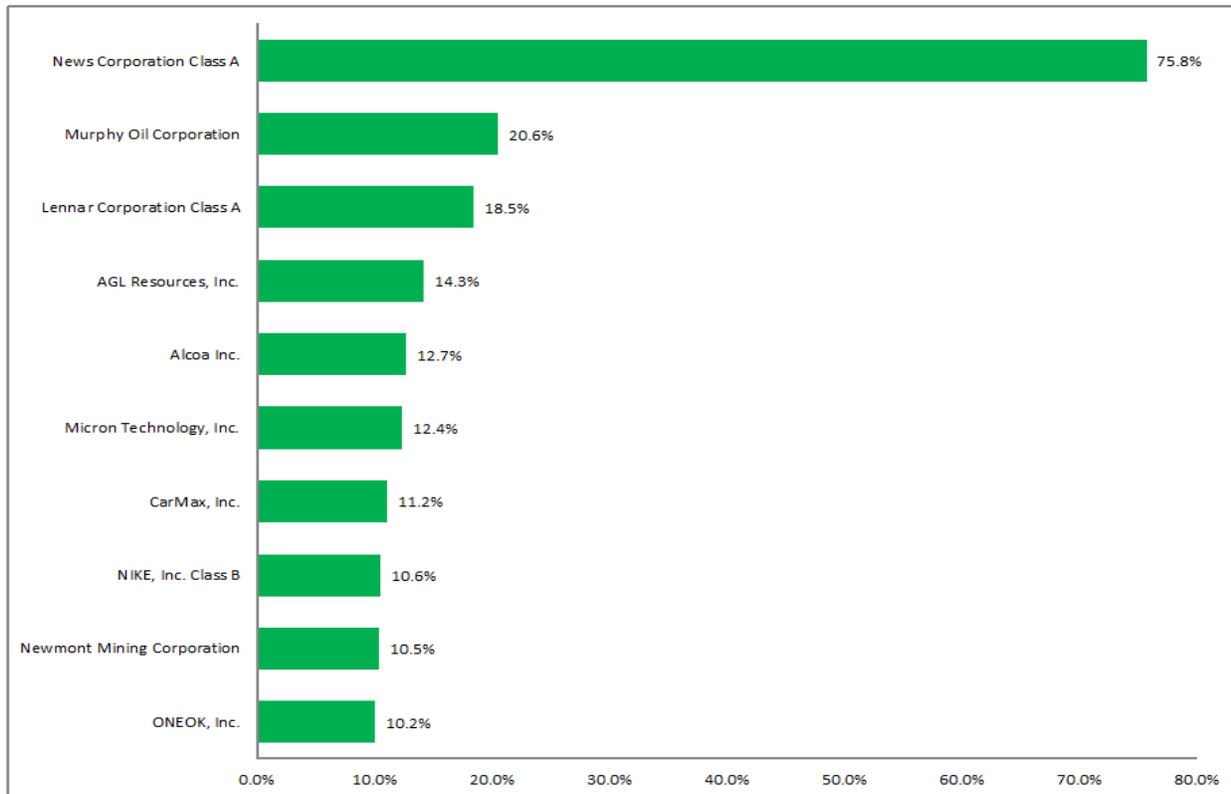


Percentage of Positive & Negative EPS Preannouncements: Q3 2013

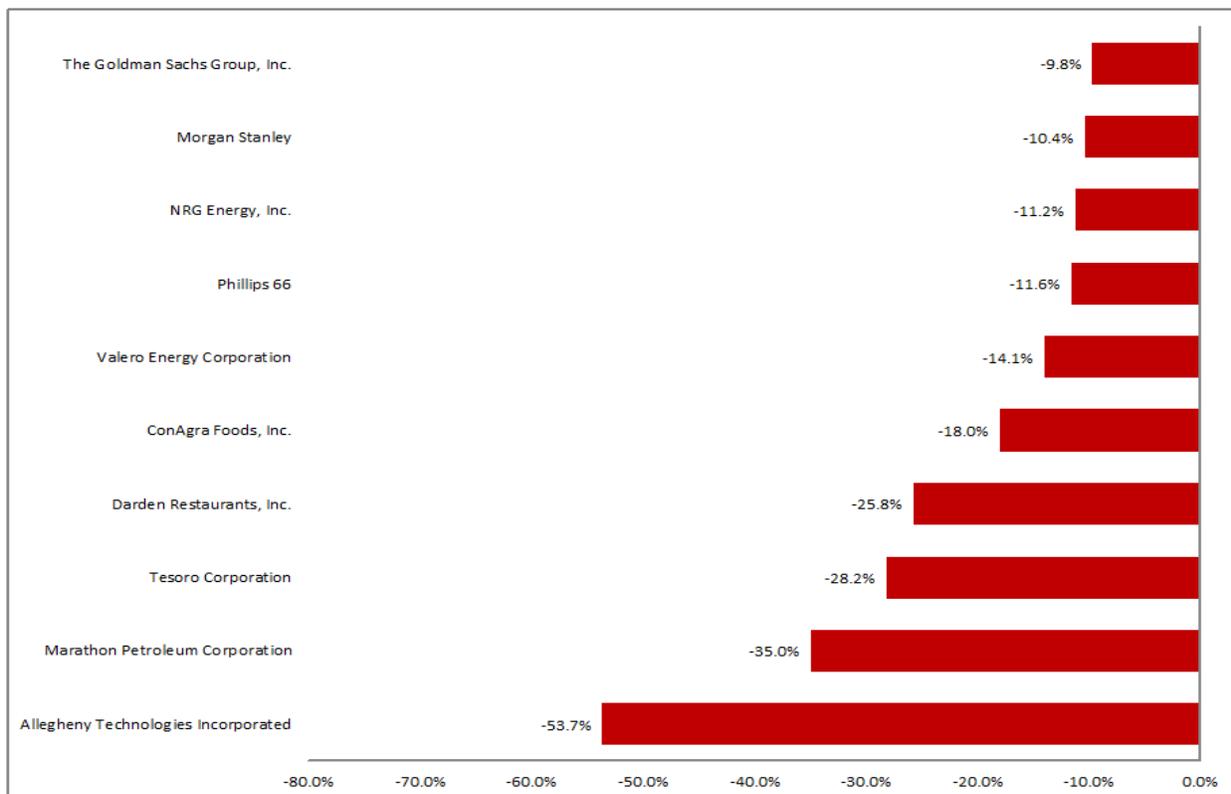


### Q3 2013: EPS Revisions

Highest Upward Change (Trailing 4-Weeks) in Mean EPS Estimate: Top 10 Companies

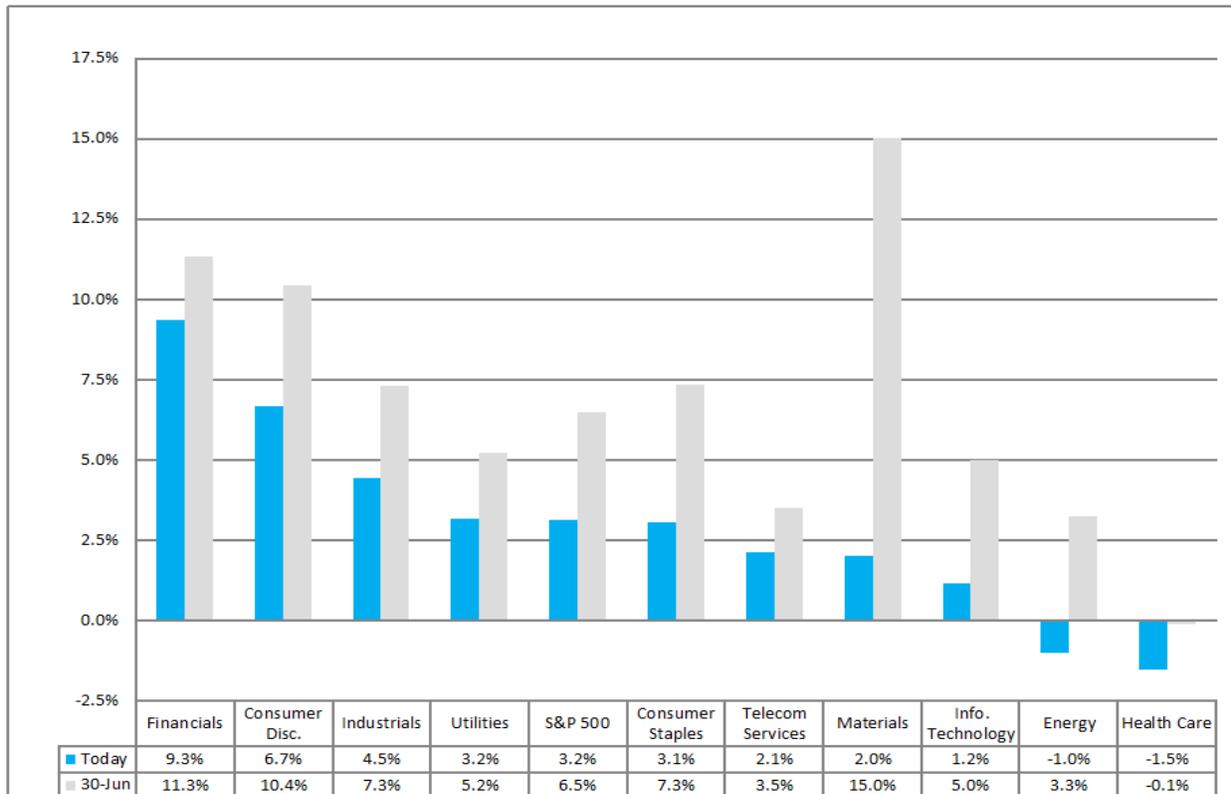


Highest Downward Change (Trailing 4-Weeks) in Mean EPS Estimate: Top 10 Companies

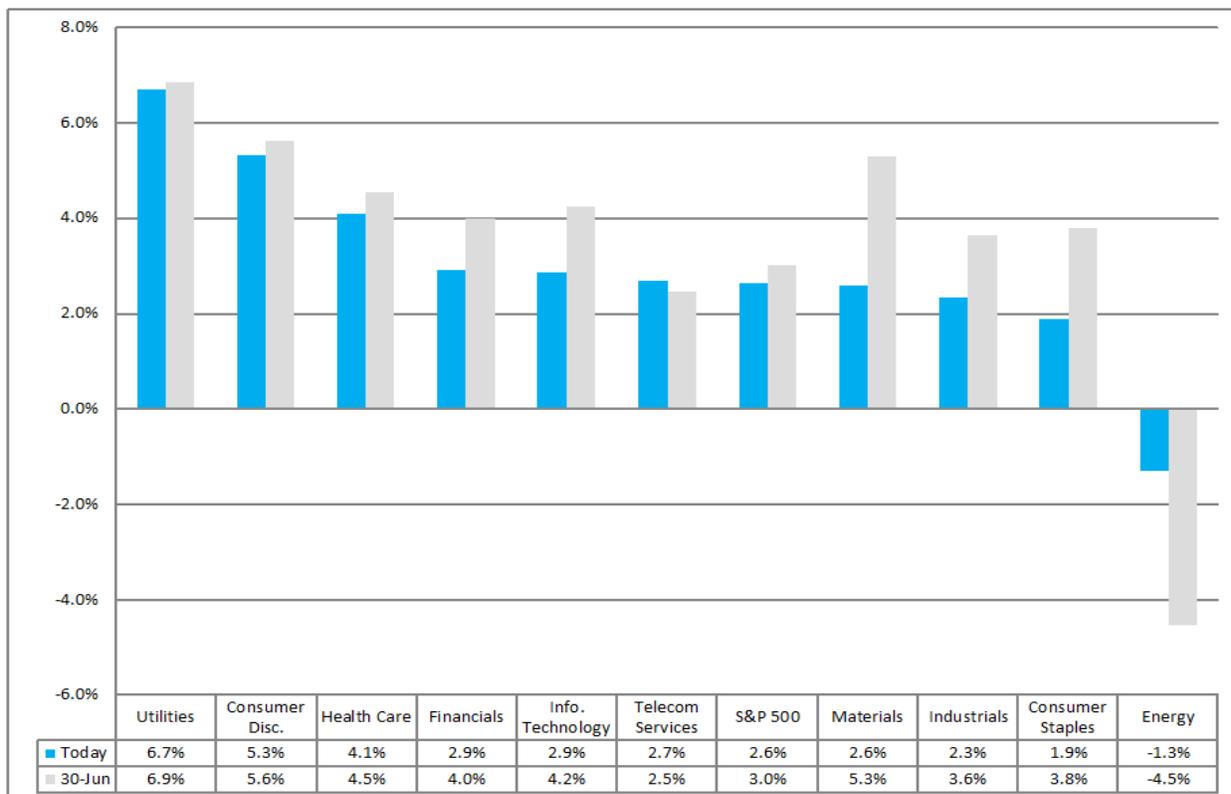


Q3 2013: Growth

Q3 2013 Earnings Growth

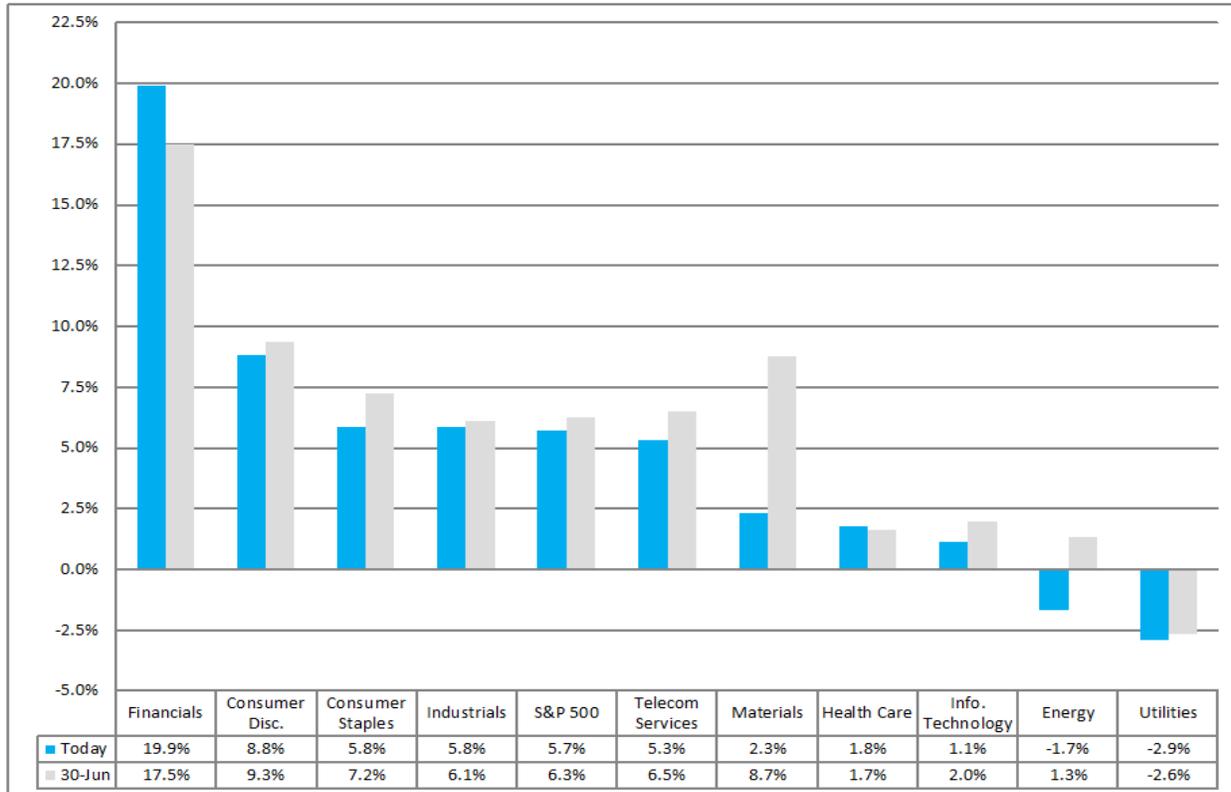


Q3 2013 Revenue Growth

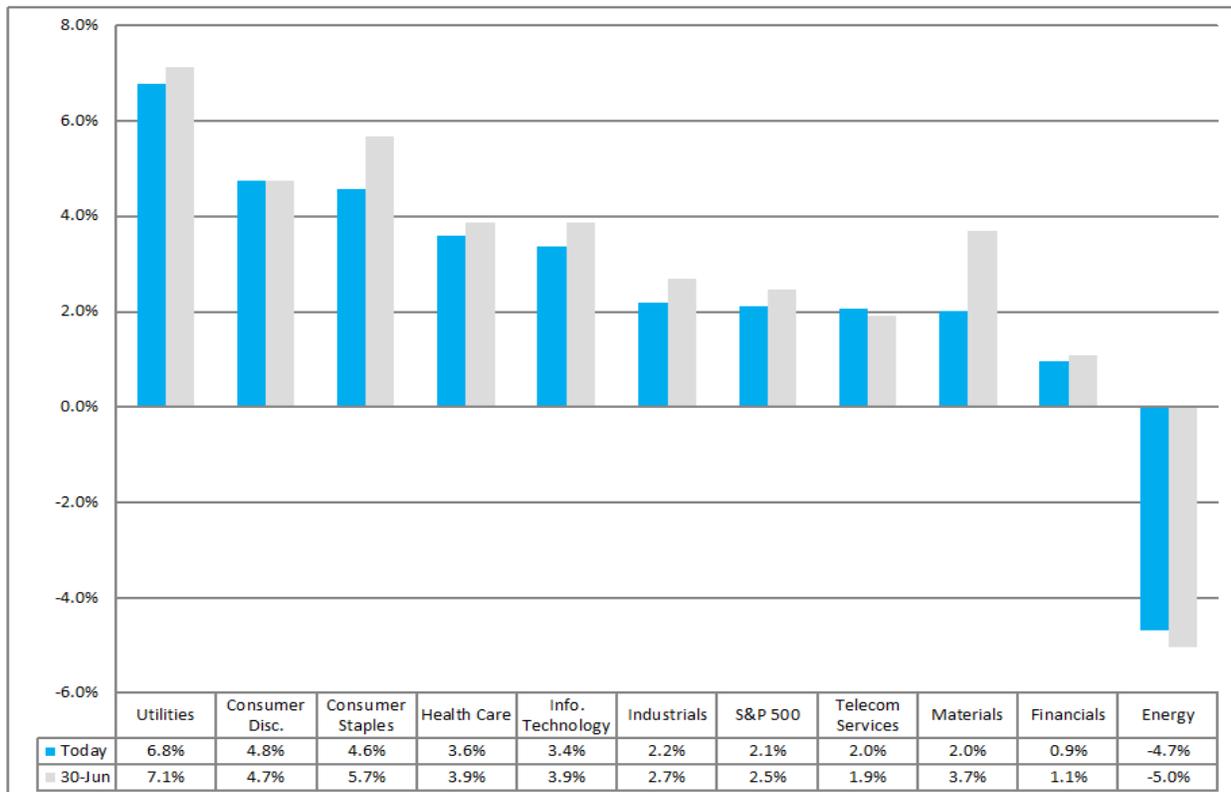


CY 2013: Growth

CY 2013 Earnings Growth

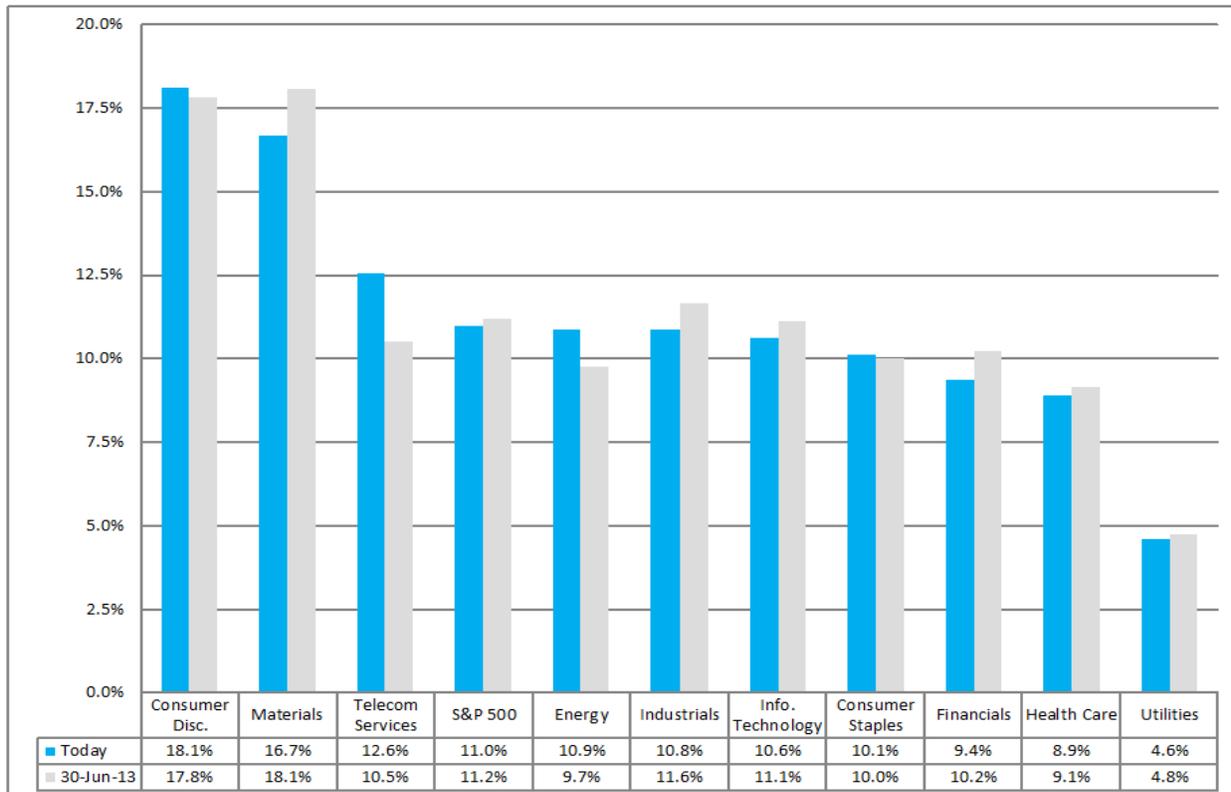


CY 2013 Revenue Growth

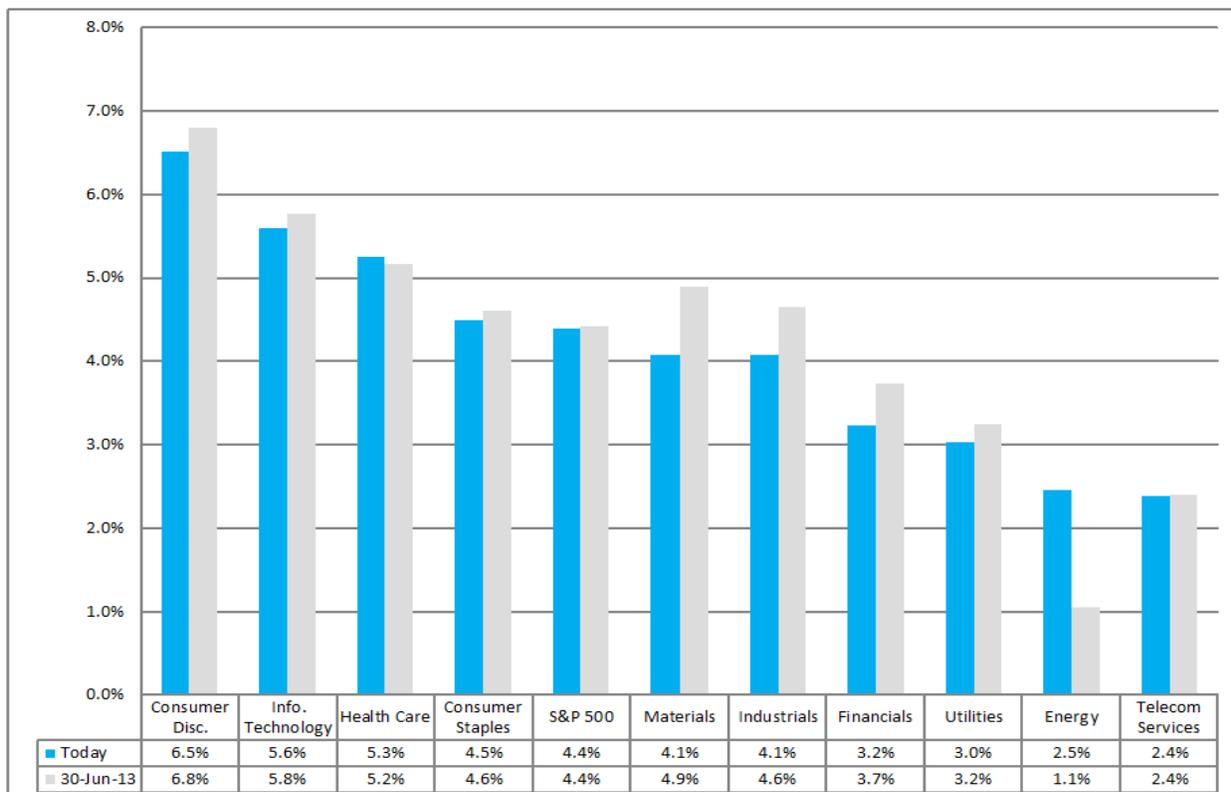


CY 2014: Growth

CY 2014 Earnings Growth

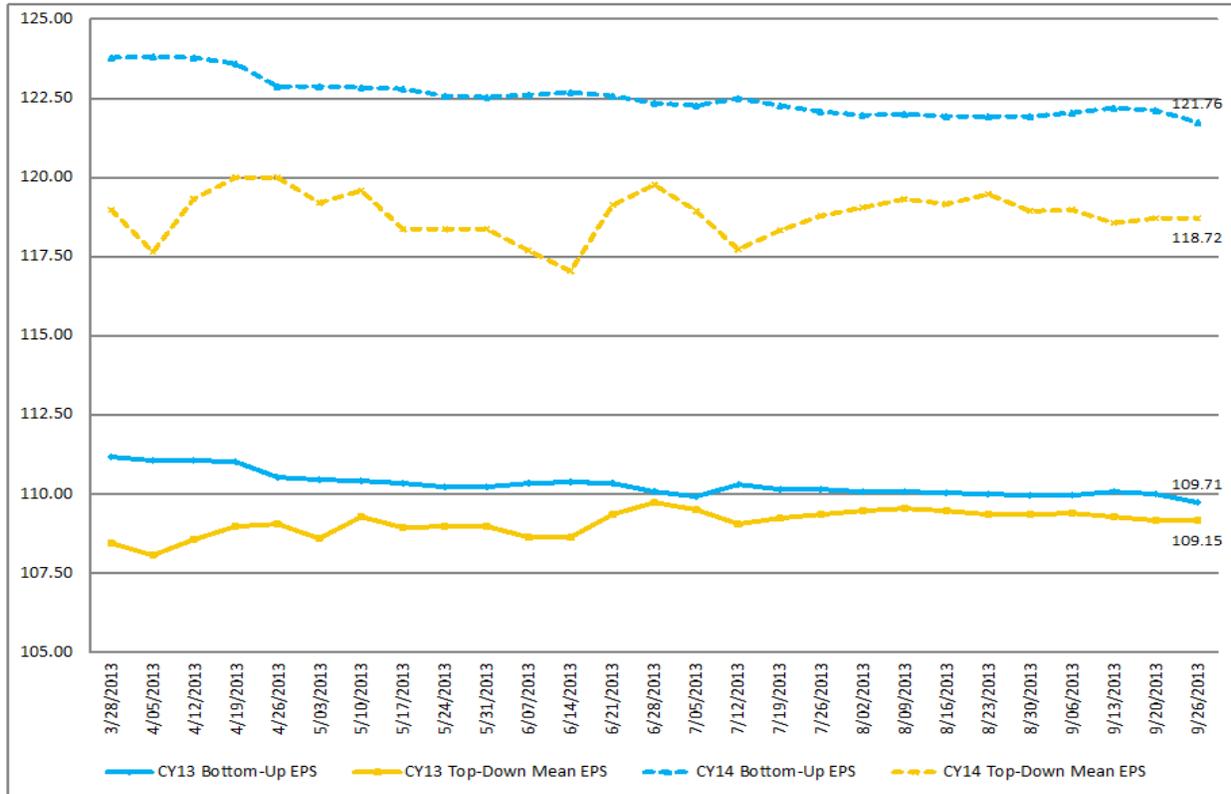


CY 2014 Revenue Growth

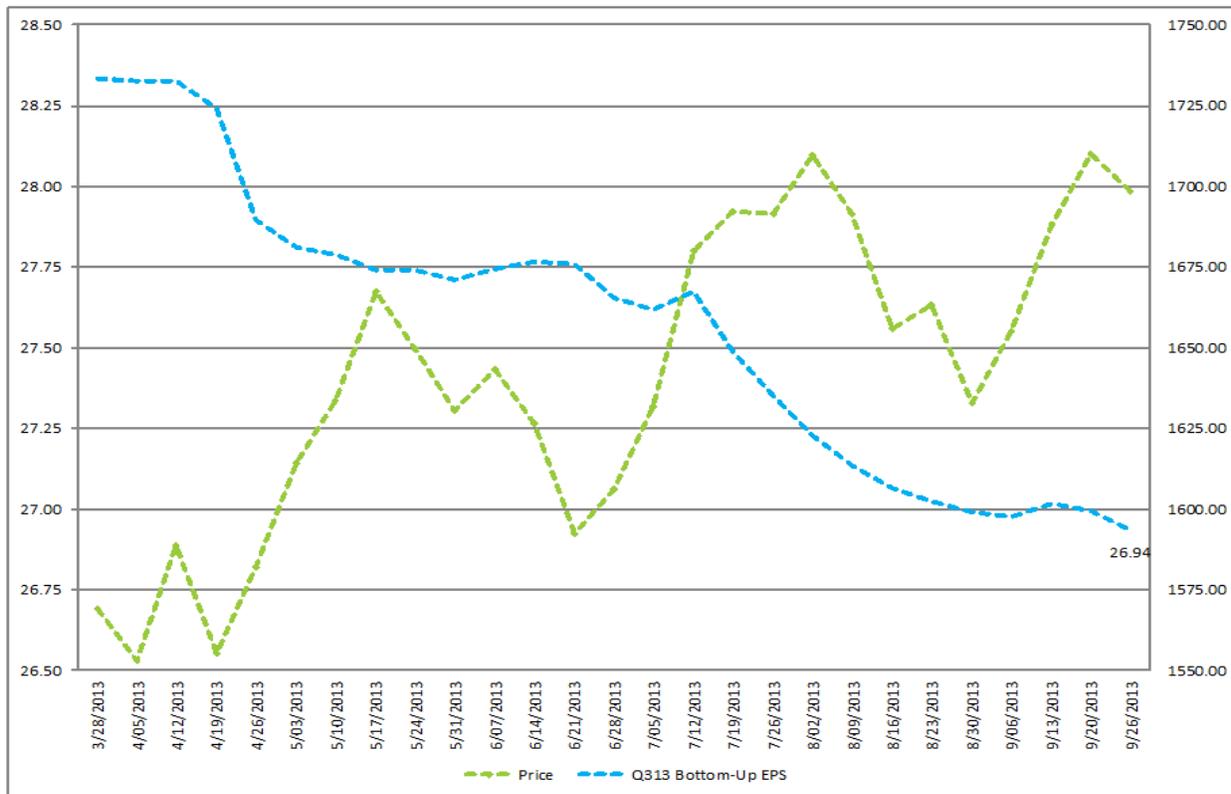


## Bottom-up EPS Estimates: Revisions

CY Bottom-Up EPS vs. Top-Down Mean EPS (Trailing 26-Weeks)

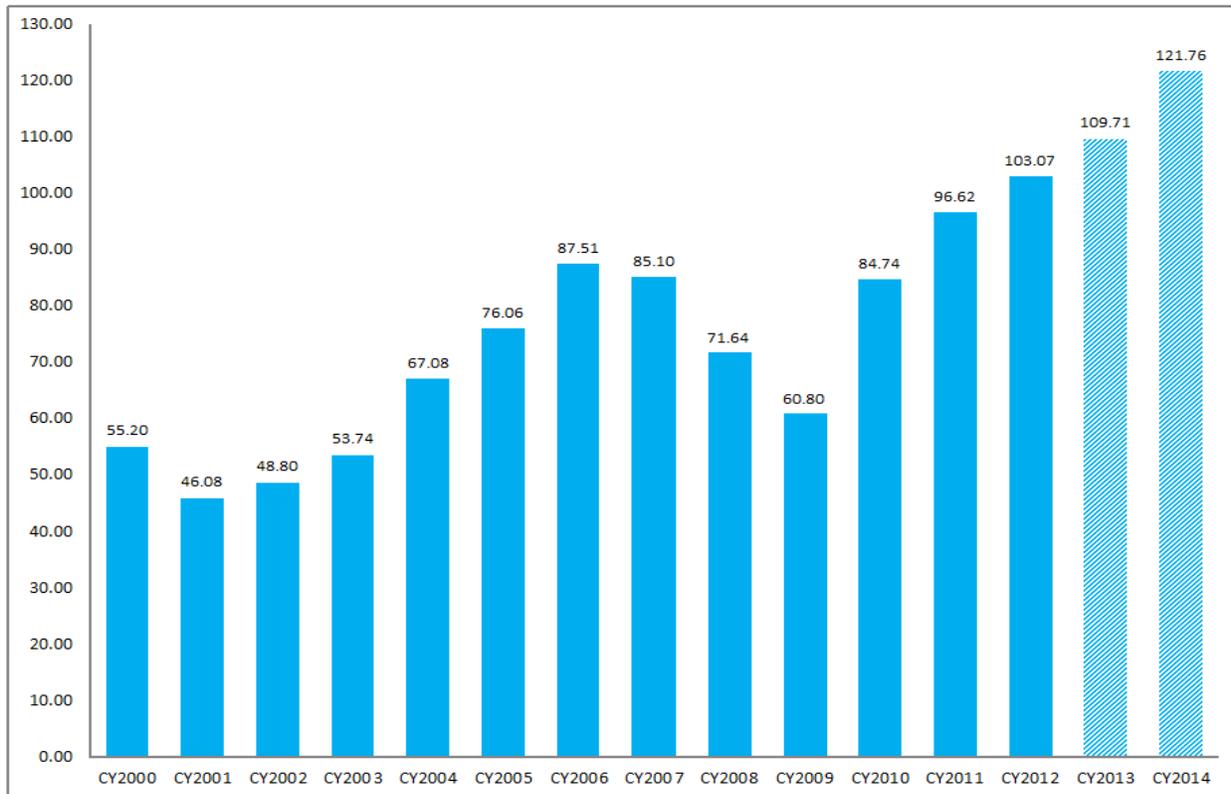


Change in Q213 Bottom-Up EPS vs. Price (Trailing 26-Weeks)

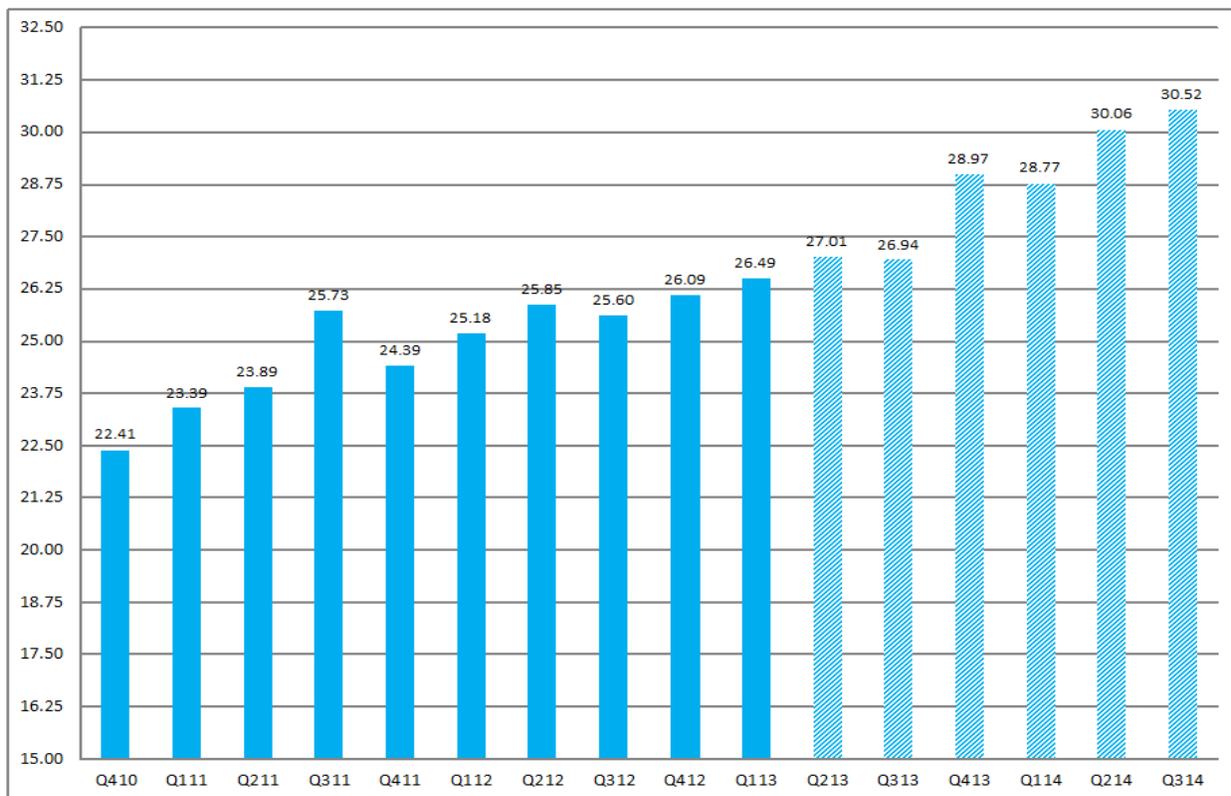


## Bottom-up EPS Estimates: Current & Historical

Calendar Year Bottom-Up EPS Actuals & Estimates

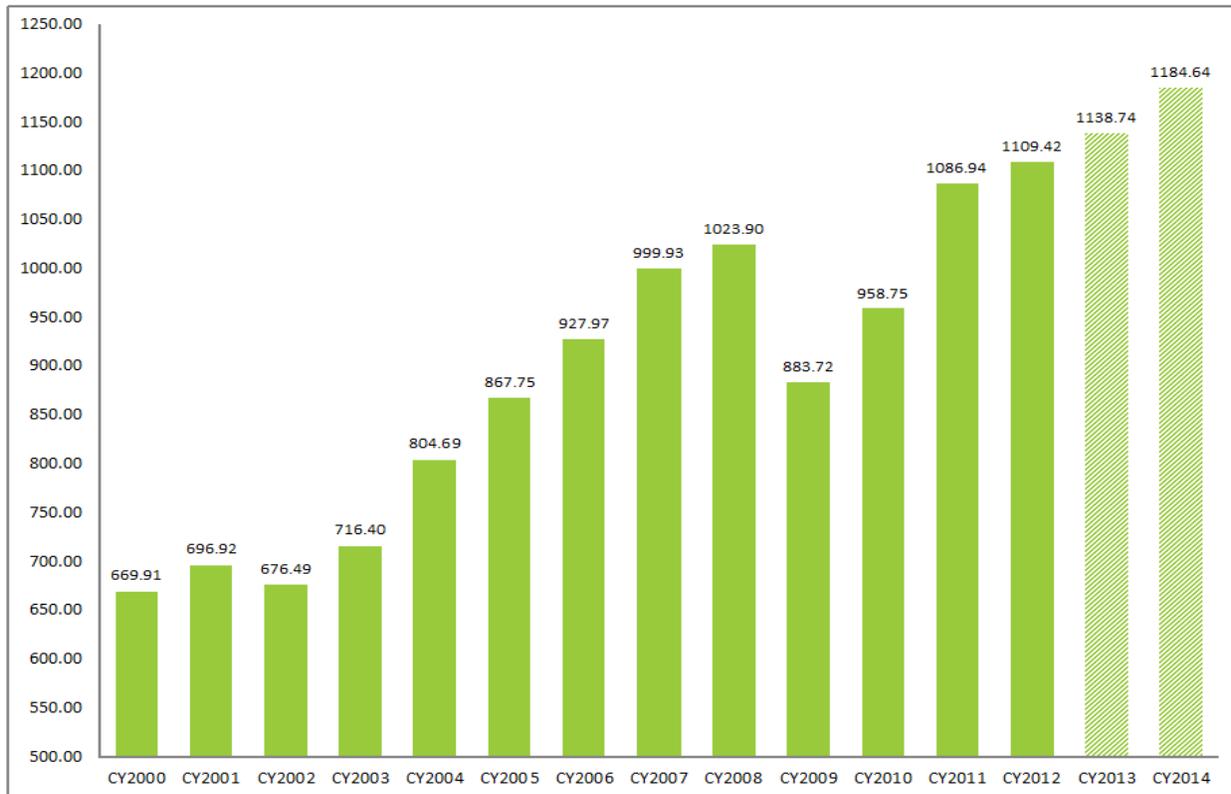


Quarterly Bottom-Up EPS Actuals & Estimates

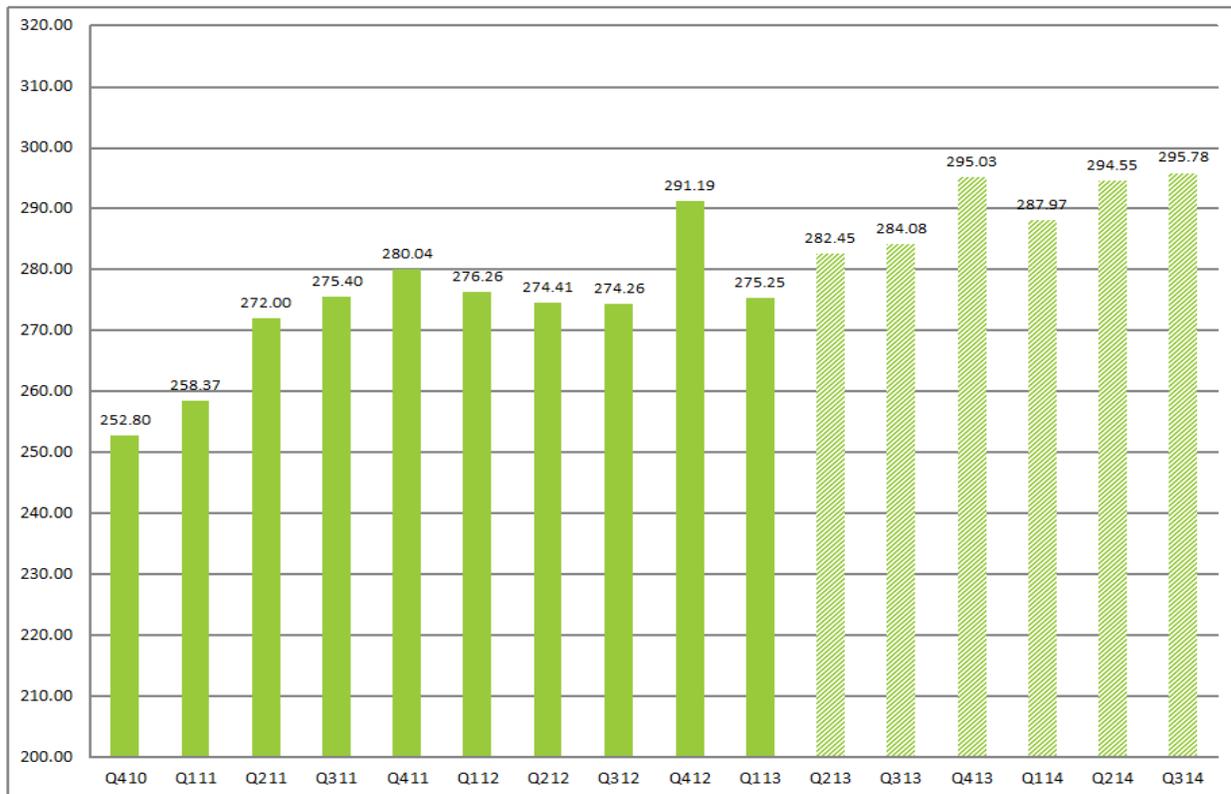


## Bottom-up SPS Estimates: Current & Historical

Calendar Year Bottom-Up SPS Actuals & Estimates

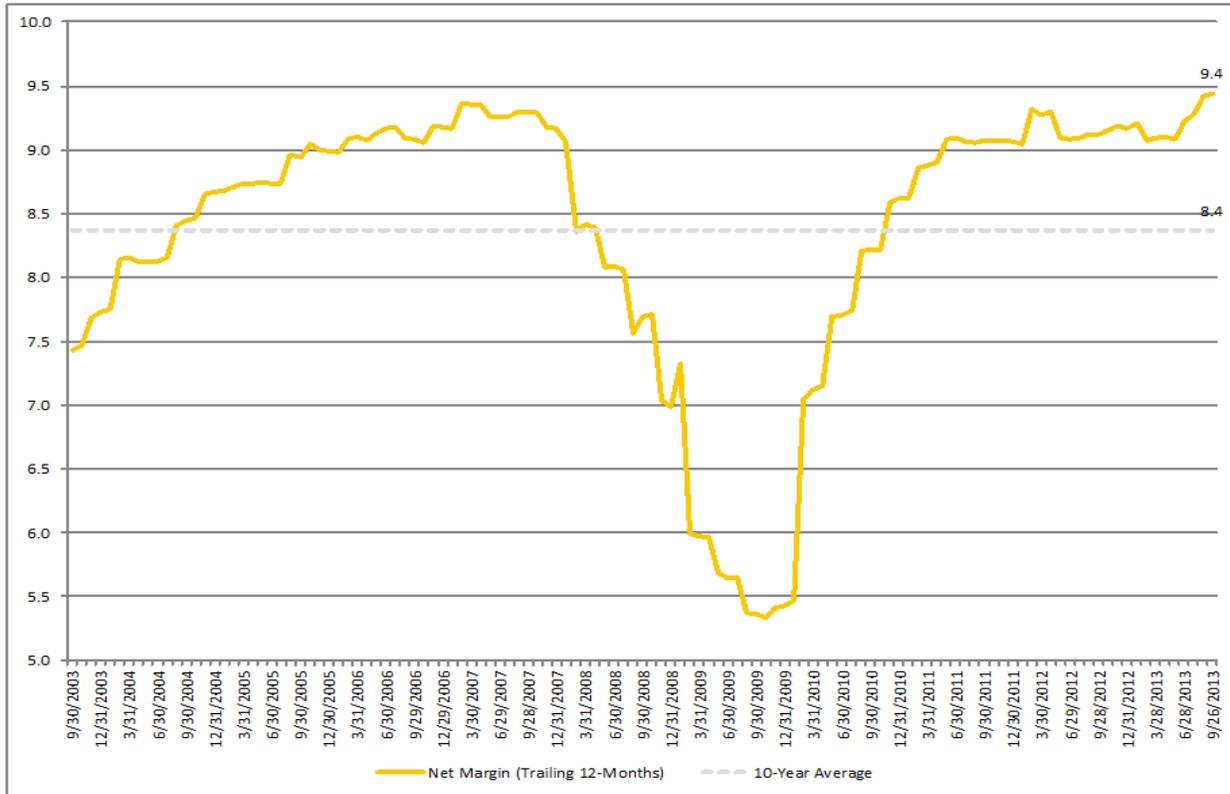


Quarterly Bottom-Up SPS Actuals & Estimates

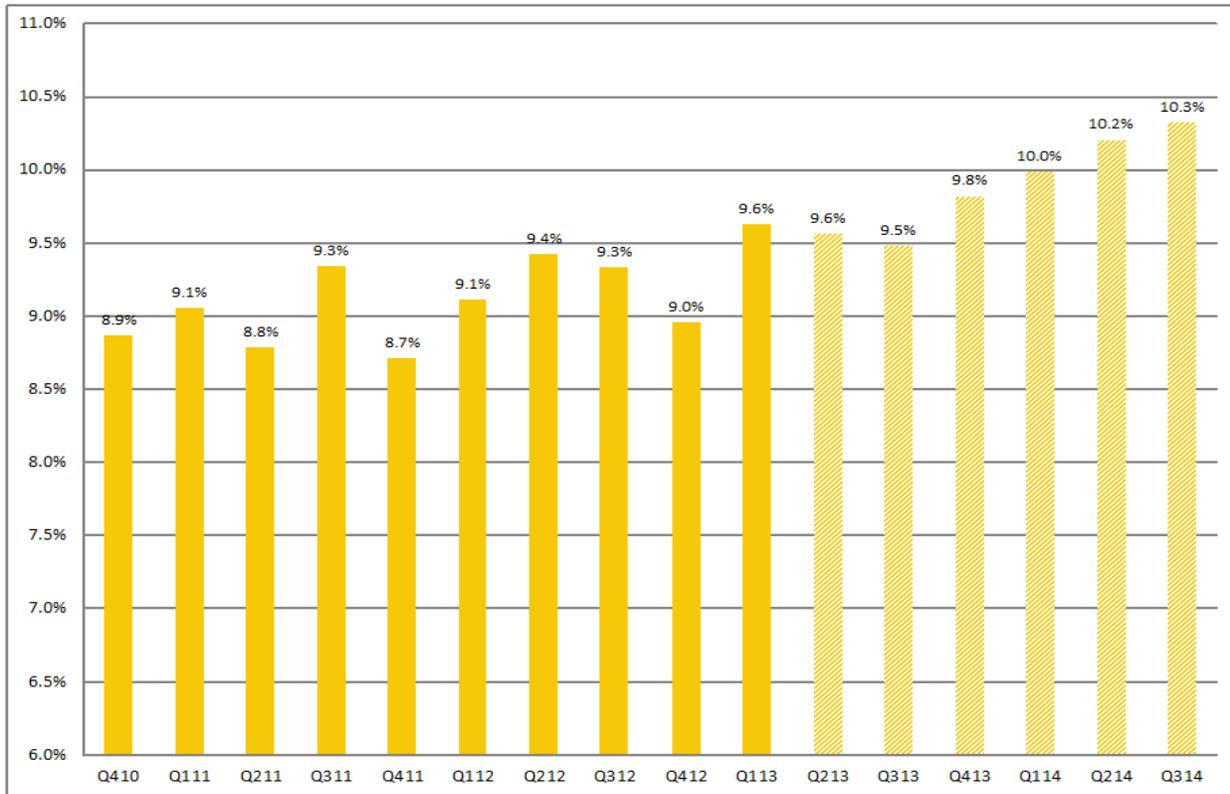


## Net Margins: Current & Historical

Trailing 12M Net Margin: 10 Years

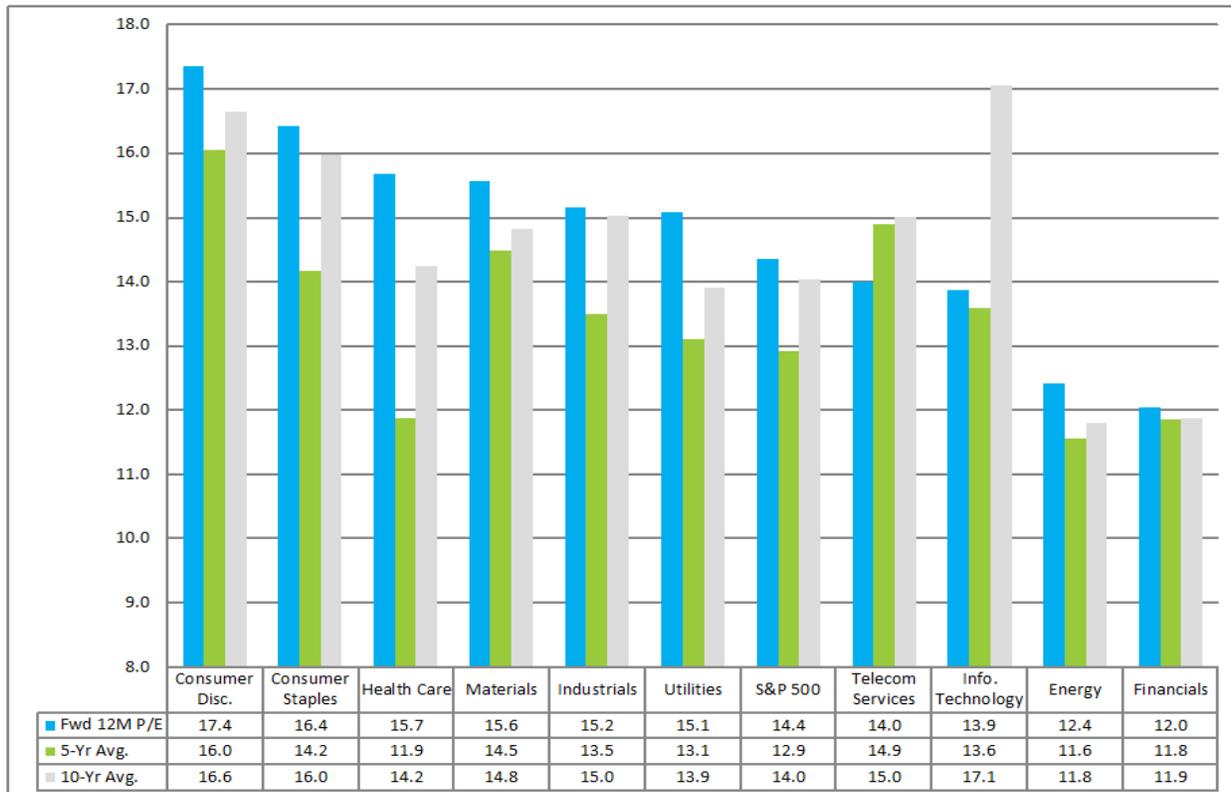


Quarterly Net Margins (Bottom-Up EPS / Bottom-Up SPS)

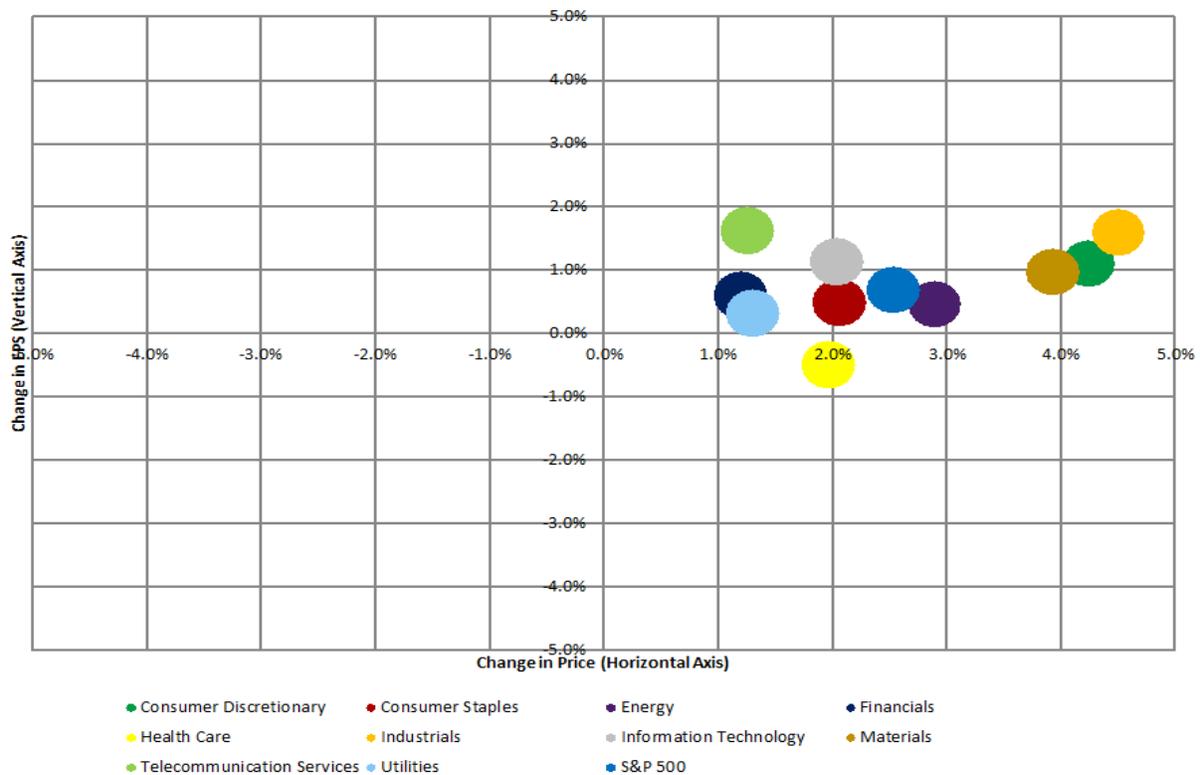


## Forward 12M Price / Earnings Ratio: Sector Level

Sector-Level Forward 12-Month P/E Ratios

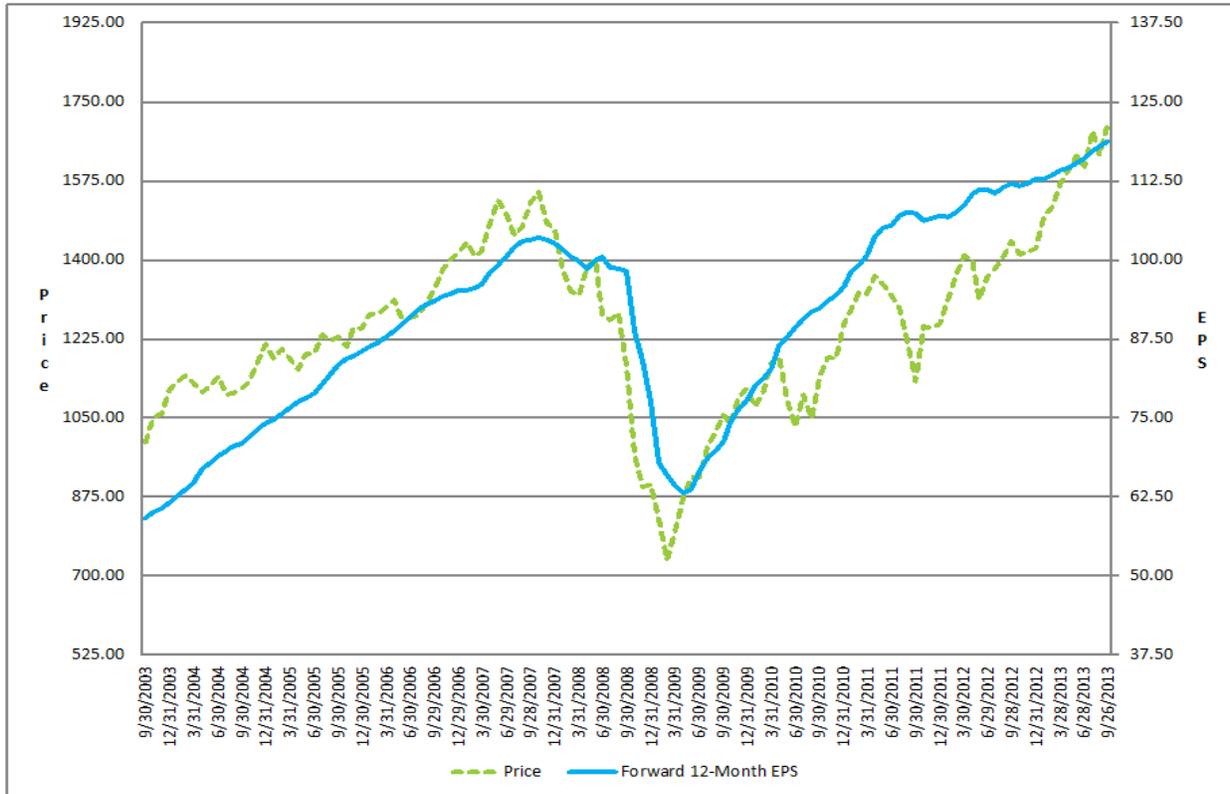


Sector-Level Change in Price vs. Change Forward 12M EPS: 1-Month

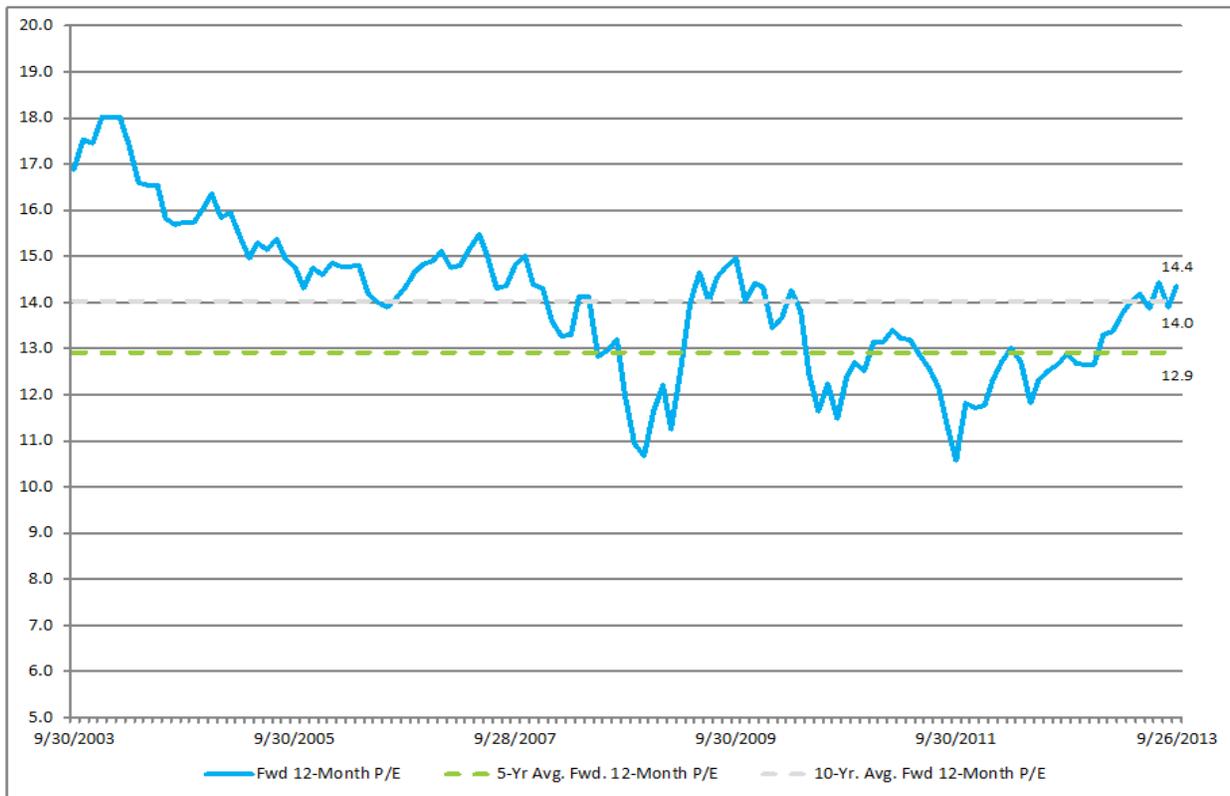


## Forward 12M Price / Earnings Ratio: Long-Term Averages

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

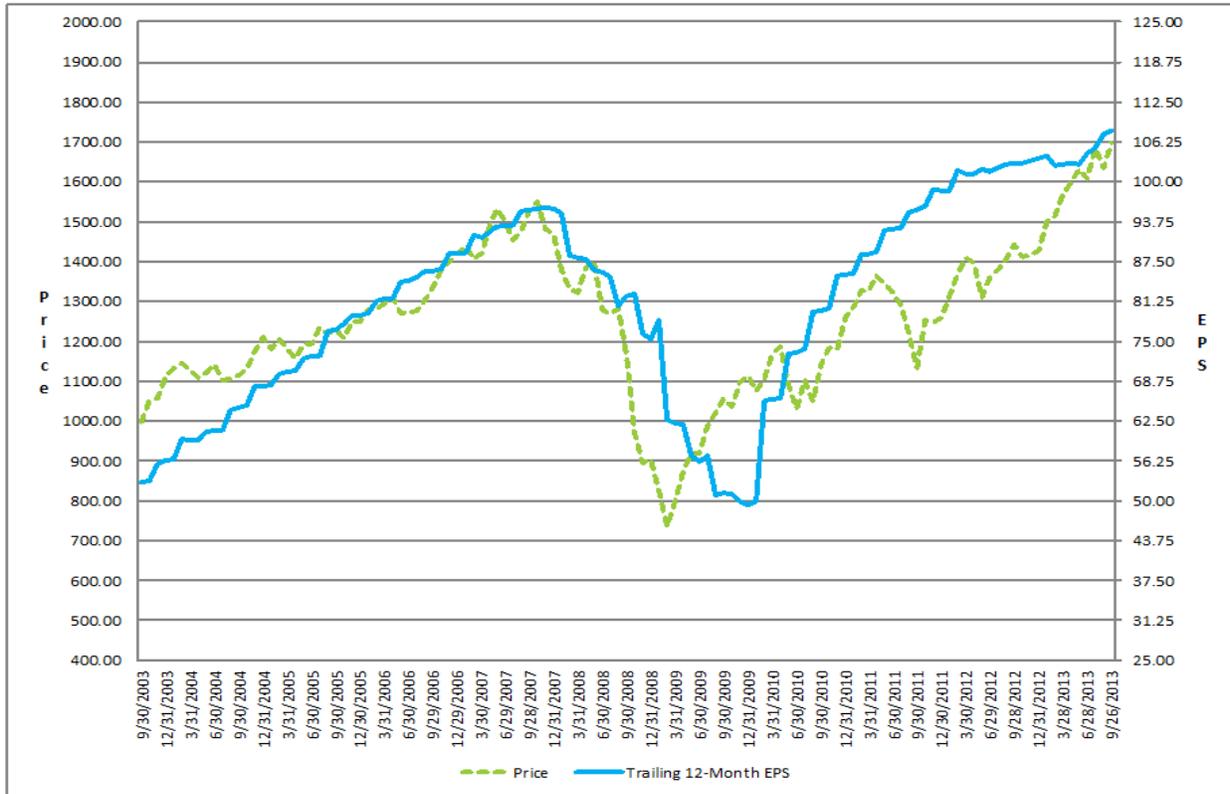


Forward 12M P/E Ratio: 10-Year



## Trailing 12M Price / Earnings Ratio: Long-Term Averages

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



Trailing 12M P/E Ratio: 10-Year



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