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Ibra WANE,
Senior Equity Research Strategist



Debora DELBO',
EM Macro Strategist

A multi-speed earnings season in some regions, but above expectations everywhere

Less impacted by the pandemic, Japanese and emerging market results are one step ahead

Q4 earnings season: an impressive resilience that supports our pro-cyclical views

Given the context, Q4 2020 corporate earnings proved resilient. The regions least impacted by the pandemic, such as EM (+25%) and Japan (+20%), experienced notable increases. In the rest of the world, where the pandemic was more virulent, the US still managed to post a positive gain (+4%) while Europe was more affected (-20%). However, even in the most affected regions, the results were far better than expected, with the most significant progress coming from cyclical sectors.

S&P 500: A much stronger than expected Q4 2020, with Financials and the GAFAMs on the forefront

In the US, of the 80% of S&P 500 companies that had already reported as of February 19, Q4 2020 Blended Earnings (reported + estimates for the remaining) are now seen growing by +3.7%, which is much better than what was expected at the start of the year (-10.3%). Likewise, this marks an improvement versus Q3 (-6.5%) which was not obvious, given the worsening of the sanitary context and the slowdown of the US economy at the end of the year.

From one sector to another, developments were, however, very fragmented, with three sectors in particular that stood out on the rise (Technology + 19%, Financials + 21% and Materials + 22%) and two on the decline (Industry -37% and Energy -105%). But it was above all the analysis of the gaps that was revealing. Thus, while good or bad, the results had been well anticipated in most sectors. It was mainly Financials and Technology in the broad sense that thwarted (in the upward direction) all forecasts.

Between the good performance of market activities and lower provisions than expected, Financials' results thus increased by + 21%, instead of the expected -7%.

But it was once again from the GAFAMs that the surprise came. GAFAMs, which can be found in both IT (Apple and Microsoft), Consumer Discretionary (Amazon) and Communication Services (Google and Facebook), saw their Q4 results jump by + 41%, against + 12% expected.

Stoxx 600: Given the context, Q4 results proved relatively resilient. H1 2021 could be at risk but H2 should be significantly better

In Europe, where nearly 45% of the Stoxx 600 companies had reported as of February 16, results have gradually improved. Whereas on January 1, the consensus was for a decline of -27% in Q4, it was only -20% on February 16. Likewise, the proportion of results exceeding analyst estimates was very high, with a gross and net ratio of 66% and 32% (balance of results above expectations vs. below or

match), far ahead the average of the past ten years (respectively 51% and 2%!).

The most significant increases were recorded in cyclical sectors such as Basic Materials (+ 60%) and Consumer Discretionary (+22%). These two sectors also stood out very favourably in terms of earnings surprises, with results respectively +26% and +31% better than expected on January 1. In addition, other cyclical sectors whose results fell in Q4, such as Financials (-40%) or Industrials (-45%) did much better than expected, at respectively +11 and + 9%.

Given the improving environment and the easy comparisons, Stoxx 600 results should strongly rebound in 2021. But between the timid ramp-up of vaccination campaigns (with the exception of the UK) and the maintaining of severe restrictions, this rebound could be weaker than expected and partly delayed to H2 2021. However, even if the European recovery were to be delayed by some months, it should take hold. Therefore, in our view, without deviating from quality entirely, we should already look at cyclical sectors.

Relatively isolated from the pandemic, Japan's results proved impressive

In Japan, where 98% of MSCI companies have already reported, progress has been even more impressive, with an optical increase in earnings of + 38%! In reality, once restated for Softbank's windfall profits, the core earnings rebound was closer to 20% which remains incomparably better than the cautious consensus expectations of January 1st (drop of -15%). By sector, it is again in Cyclical where progress was the strongest, with an average increase of + 23%, and peaks beyond 50% in Technology, Banks or Building Materials, while sectors deemed Defensives recorded an average increase of + 11% excluding Softbank.

Emerging markets' earnings season is not yet very far along but already looks promising

Although with only 27% of MSCI EM companies have reported as of February 17th (Source: Capital IQ), the first indications are very encouraging with,

THEMATIC

Given the prospect of an accelerating recovery, enthusiasm for growth stocks should decrease

overall, a double-digit earnings growth (in USD, +45% reported and +25% blended) and +7.5% higher than on January 1st.

By country, the biggest gainers were Malaysia (+400%, thanks to the Health Care sector, but still only 21% of the companies reported), Korea (+99%, with 60% of the companies already reporting) and Saudi Arabia (+89%, with 39% of the companies already reporting). On the other hand, Poland, United Arab Emirates, Qatar, Indonesia, Philippines and Thailand continue to post negative earnings growth. At the sector level, Health Care, Materials and Consumer Discretionary made a strong showing on average on all the countries.

Our expectations for 2021 have been revised further up (from 16% to +24% in USD). From a regional standpoint, earnings growth in the first half of 2021 will be more concentrated in Emerging Asia, more resilient in the recovery and much more linked to booming e-commerce profits. The laggards, starting with EMEA (Russia) and then Latam, are unlikely to return to positive YoY numbers until the second half of 2021.

These good results received without real enthusiasm could become an opportunity...

Overall, the Q4 earnings season has proven to be remarkably resilient. However, these good results have been met with mixed reactions.

This is particularly the case in the US, where, within a few weeks market concerns have shifted from doubts about the recovery to a possible overheating, or even a revival of inflation. In response, long yields tightened. The UST 10-year yield, for example, surged from 0.9% at the start of the year to 1.20% in mid-February and could range between 1.50 to 1.8% over the year according to our central scenario.

If it goes not substantially higher than that, this should favour rotation but do little to hamper the equity markets. In the US, from a thematic point of view, this would confirm our preference for Small Caps and Value, which should be the main beneficiaries of the recovery. Conversely, in such a context, Growth and Quality would be less sought after. In Europe, Small Caps and Value should also benefit from the recovery. However, as the recovery is not as far along as in the United States (due to greater restrictions and delays in vaccination) and doomed to remain weaker (due to less stimulus), we will also continue to focus on Quality.

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