S&P 500 EPS Outlook

Entering a virtuous cycle – raising S&P 500 EPS

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Raising 2024 EPS to $250, launching 2025 at $275

We raise our 2024 S&P 500 EPS estimate to $250 (+12% YoY; vs. $235 previously), the highest top-down forecast on the Street. Companies delivered another strong beat in 4Q (see 4Q earnings) and our economists raised their 2024 GDP forecast to +2.7% YoY (vs. +1.4% in November). The 1.3ppt increase in GDP forecast translates to a 5ppt boost to EPS growth, all else equal. 2023 was a transition year for Corporate America, and companies have now adjusted to the new higher rate and tepid demand environment. Our top-down framework suggests EPS undergrew by 3ppt in 2023, which should be recouped in 2024. We also launch our 2025 EPS forecast at $275 (+10% YoY). See our S&P EPS model.

AI's virtuous investment cycle

Hyperscalers (MSFT (Microsoft), AMZN (Amazon), GOOGL (Alphabet), META) are expected to spend $180B on capex in 2024E, +27% YoY (Exhibit 17). The $38B YoY increase in capex of represents ~80% of their expected earnings growth YoY – i.e., they're entering a reinvestment cycle. History suggests companies in reinvestment cycles underperform (Exhibit 20), but we see a potential virtuous cycle forming from AI (artificial intelligence) investments. Semis and networking are the most obvious beneficiaries (Exhibit 19), but increased power usage and the physical build-out of data centers will lead to more demand for electrification, utilities, commodities, etc. (see AI impact to Industrials, Utilities, Data Center REITs). Productivity gains from AI and domestic investments are also a major tailwind (Exhibit 26).

New economy is investing, old economy is cutting back

Excluding the hyperscalers, S&P 500 capex is expected to grow at just 1% YoY. This is the opposite of last year's trend when hyperscalers cut back 7% on capex, while the others increased capex by 9% YoY. Similarly, whereas Tech layoffs peaked last year, layoffs remain elevated in other sectors (Exhibit 14). As Big Tech enters an investment cycle and the old economy cuts costs/capex, we expect to see the growth differentials merge between Tech and the others (see Exhibit 34).

EPS cycle is different from the economic cycle

Goods/manufacturing represent 50% of earnings but just 20% of the economy (Exhibit 7). Hence, the post-COVID shift from goods to services resulted in an EPS recession despite above-trend GDP in 2023 (Exhibit 8). But we see continued signs of a manufacturing upcycle, signaling an end to the third-longest manufacturing downturn in history (Exhibit 9). Inventory levels are now just back to normal (Exhibit 10) and a re-stocking cycle could be next (see Truckers). Historically, when the ISM manufacturing PMI has been in expansion, S&P 500 EPS have grown 12% on average.

Risks: weaker demand & potential tariffs

Demand recovery will be the key driver of earnings in 2024-25. Although margins recovered from the lows on lower costs, further margin gains will need better demand. Potential tariffs in the event of a Trump victory in the presidential election are another key risk – e.g., assuming no price pass-throughs, we estimate a 5% EPS hit from 60% tariffs on Chinese imports, all else equal.

Exhibit 1: 2024-25 EPS forecast
BofA vs. consensus EPS forecast

	Btm-up analysts	YoY	BofA Strategy	YoY
1Q23	53.08	-3%	53.08	-3%
2Q23	54.29	-6%	54.29	-6%
3Q23	58.41	4%	58.41	4%
4Q23E	57.24	8%	57.24	8%
2023E	**$222**	**2%**	**$222**	**2%**
1Q24E	55.17	4%	57.00	7%
2Q24E	59.32	9%	61.00	12%
3Q24E	63.59	9%	65.00	11%
4Q24E	65.27	14%	67.00	17%
2024E	**$243**	**10%**	**$250**	**13%**
2025E	**$276**	**13%**	**$275**	**10%**

Source: FactSet, BofA Equity & Quant Strategy
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Exhibit 2: BofA Strategy 2024 EPS vs. top-down consensus
BofA vs. top-down strategists

BofA	**$250**
Top-down avg.	$235
Median	$235
High	$250
Low	$220
Sample size	21

Source: Bloomberg
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S&P 500 EPS outlook

Raising 2024 EPS to $250, launching 2025 at $275

We raise our 2024 S&P 500 EPS estimate to $250 (+12% YoY) from $235 previously (+6% YoY), the highest top-down forecast on the Street. Companies delivered another strong 5% beat in 4Q (see earnings tracker) and our economists raised their GDP forecast to +2.7% YoY in 2024 (vs. +1.4% in November). The 1.3ppt increase in GDP forecast translates to a 5ppt boost to EPS growth, all else equal. We also launch our 2025 EPS forecast at $275 (+10% YoY).

Exhibit 3: We expect 12% EPS growth in 2024, followed by 10% growth in 2025 – see our excel model
BofA S&P 500 EPS outlook

All based on current constituents unless specified		**Bottom-up Consensus**				**BofA Analyst estimates**				**BofA Strategy**			
	2023	2024	*y/y*	2025	*y/y*	*2024*	*y/y*	2025	*y/y*	*2024*	*y/y*	*2025*	*y/y*
S&P 500 Pro-forma EPS (Historical Index)	$222.0												
S&P 500 Pro-forma EPS (Current Constituents)	$224.1	$243.4	*9%*	$276.0	*13%*	$247.0	*10%*	$279.9	*15%*	$250.0	*12%*	$275.0	*10%*
Sector ($ billions)													
Consumer Discretionary	157.8	171.2	*9%*	196.1	*15%*	198.4	*26%*	225.0	*31%*	179.3	*14%*	196.1	*9%*
Consumer Staples	122.0	127.1	*4%*	136.7	*8%*	127.3	*4%*	136.8	*8%*	126.6	*4%*	132.0	*4%*
Energy	142.6	132.3	*-7%*	148.5	*12%*	128.9	*-10%*	144.2	*9%*	140.5	*-1%*	149.5	*6%*
Financials	337.9	329.1	*-3%*	356.8	*8%*	326.5	*-3%*	353.2	*7%*	335.3	*-1%*	359.1	*7%*
Health Care	244.5	277.3	*13%*	310.0	*12%*	277.4	*13%*	309.8	*12%*	276.7	*13%*	299.8	*8%*
Industrials	162.7	174.6	*7%*	197.5	*13%*	173.6	*7%*	196.8	*13%*	181.9	*12%*	202.0	*11%*
Information Technology	375.8	440.1	*17%*	512.7	*16%*	439.4	*17%*	515.9	*17%*	453.4	*21%*	509.9	*12%*
Materials	48.2	47.2	*-2%*	53.6	*14%*	47.3	*-2%*	54.3	*15%*	47.8	*-1%*	52.2	*9%*
Real Estate	53.1	55.8	*5%*	59.2	*6%*	57.4	*8%*	60.9	*9%*	57.6	*8%*	59.7	*4%*
Communication Services	174.6	199.4	*14%*	223.1	*12%*	207.5	*19%*	229.7	*15%*	205.3	*18%*	223.4	*9%*
Utilities	52.7	59.2	*12%*	64.1	*8%*	58.9	*12%*	64.8	*10%*	60.1	*14%*	65.9	*10%*
S&P 500	1,871.9	2,013.4	*8%*	2,258.2	*12%*	2,042.6	*9%*	2,291.3	*14%*	2,064.6	*10%*	2,249.6	*9%*
S&P 500 ex. Financials	1,534.0	1,684.2	*10%*	1,901.5	*13%*	1,716.1	*12%*	1,938.1	*15%*	1,729.3	*13%*	1,890.5	*9%*
S&P 500 ex. Energy and Financials	1,391.3	1,551.9	*12%*	1,753.0	*13%*	1,587.2	*14%*	1,793.9	*16%*	1,588.8	*14%*	1,741.0	*10%*
S&P 500 ex. Energy	1,729.2	1,881.1	*9%*	2,109.7	*12%*	1,913.7	*11%*	2,147.1	*14%*	1,924.1	*11%*	2,100.1	*9%*
Energy Sector ($bn)	142.6	132.3	*-7%*	148.5	*12%*	128.9	*-10%*	144.2	*9%*	140.5	*-1%*	149.5	*6%*
Avg. Oil Price (wtd. blend of Brent & WTI)	*$81/bbl*									*~$78/bbl*	*-3%*	*~$78/bbl*	*0%*
S&P 500 Dividends (Historical Constituents, $/share)	*$70.30*									$80.00	*14%*	$88.00	*10%*
Key Macro Economic Forecasts													
Global GDP growth (real)	*3.0%*									2.9%		3.2%	
US GDP growth (real)	*2.5%*									2.7%		1.9%	
FX Rate: US$/Euro (average)	1.08									1.11		1.18	

Source: BofA US Equity & Quant Strategy, FactSet

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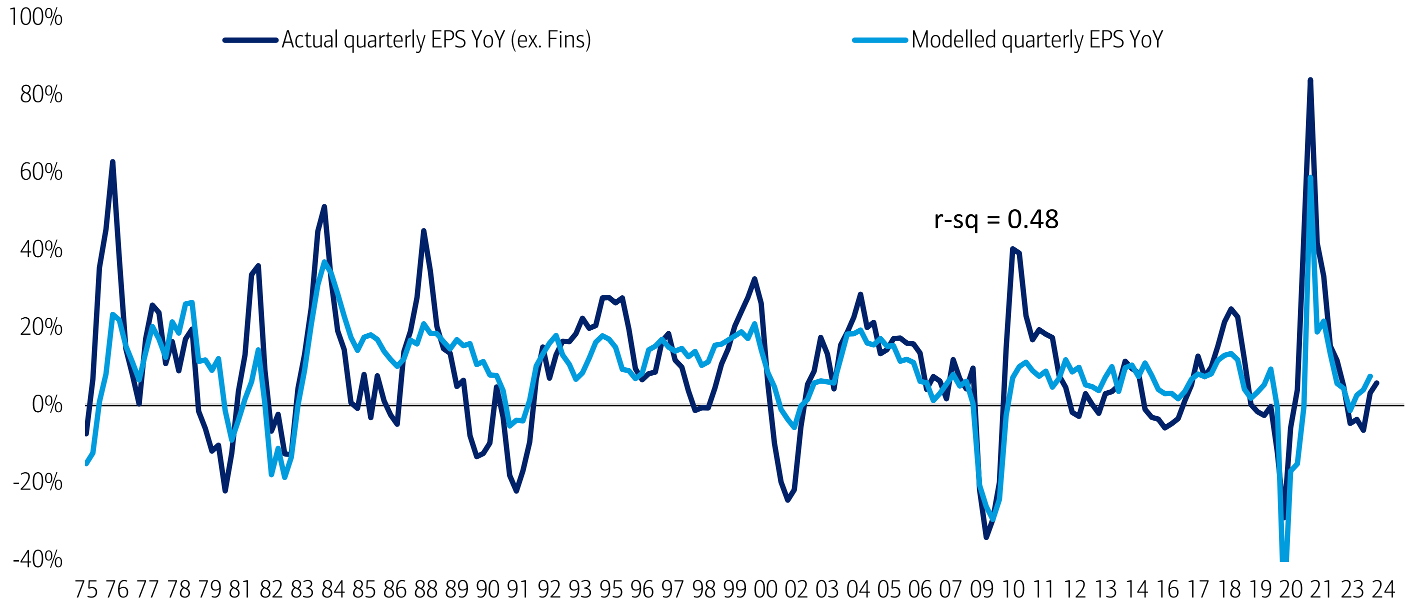
2023 was a transition year for Corporate America

2023 was a transition year for Corporate America, and companies have now adjusted to the new higher rate and tepid demand environment. Our top-down EPS framework suggests EPS undergrew by 3ppt in 2023, which should be recouped in 2024, in our view.

Exhibit 4: Actual earnings lagged top-down earnings forecast in 2023 due to higher costs and the shift from goods to services
S&P 500 quarterly EPS YoY (ex-Fins) vs. modelled EPS YoY based on linear regression using GDP (+), CPI (+), wages (-), oil (+) and USD (-)



Source: BofA US Equity & Quant Strategy, FactSet
Modelled earnings growth is based on a linear regression using these variables: GDP, CPI, Avg. hourly earnings, oil and USD

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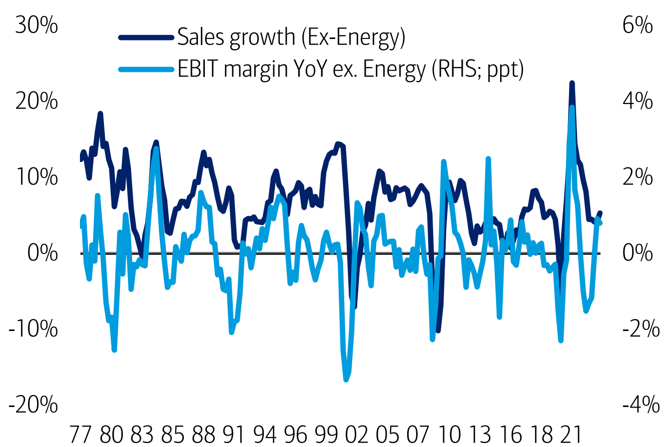
Margins bottomed, next comes demand recovery

The S&P 500 posted an 80bp rise in EBIT margins YoY, which occurred without much boost from sales. This is consistent with a typical cadence of earnings recovery, where margins usually bottom before sales start to accelerate. Once sales start to accelerate, margins typically improve even further with better operating leverage. We see two major headwinds that weighed on earnings last year reversing: manufacturing demand and cost.

Exhibit 5: Margins already inflected higher even without sales boost
S&P 500 ex. Energy & Financials sales growth YoY vs. EBIT margin YoY (1977-4Q23)



Source: FactSet, BofA US Equity & Quant Strategy

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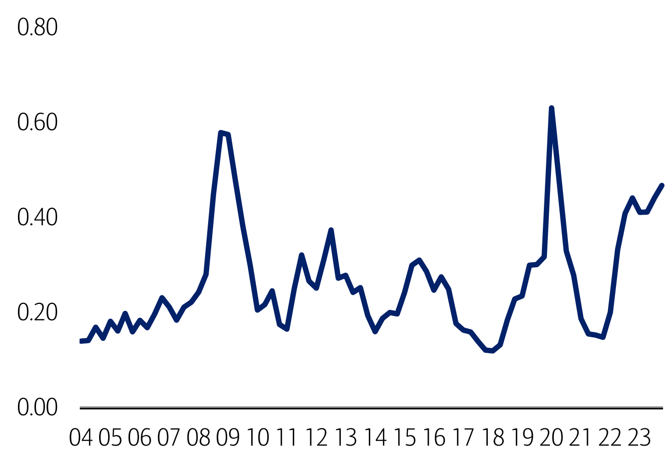
Exhibit 6: Mentions of weak demand remains elevated
Avg. mention of weak demand per company during earnings calls ('03-1Q24)



Source: BofA Global Research
Note: mentions include "lower," "softer," "moderating," "weaker"

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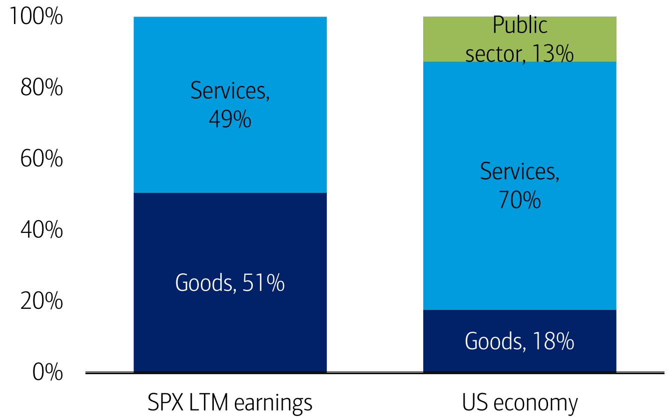
Manufacturing recession is coming to an end

Goods/manufacturing represent 50% of earnings but just 20% of the economy (Exhibit 7). Hence, the post-COVID shift from goods to services resulted in an EPS recession despite above-trend GDP in 2023 (Exhibit 8). But we see continued signs of a manufacturing upcycle, signaling an end to the third-longest manufacturing downturn in history (Exhibit 9). Inventory levels are now just back to normal (Exhibit 10), a re-stocking cycle could be next (see Truckers), and early indicators (Korean exports, rail volume) suggest a manufacturing upcycle ahead. Historically, when the manufacturing PMI has been in expansion, S&P 500 EPS has grown 12% on average on a trailing 12-mo. basis.

Exhibit 7: S&P 500 is more geared towards goods than the economy
Our estimate for Goods vs. Services exposure of S&P 500 based on industry breakout of 2Q23 earnings vs. % goods/services for US economy (based on gross value added by industry, 2022)



Source: Haver Analytics, FactSet, BofA US Equity & US Quant Strategy

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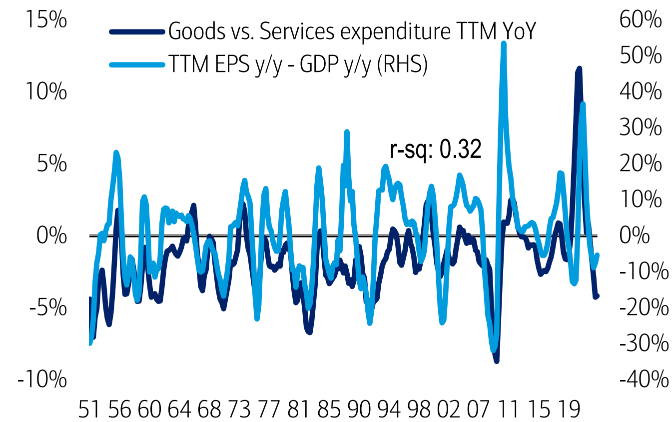
Exhibit 8: Goods outpacing services has historically been a tailwind for earnings vs. GDP
Goods vs. Services consumption TTM YoY vs. EPS vs. GDP TTM YoY (1951-4Q23)



Source: FactSet, Bloomberg, BofA US Equity & Quant Strategy

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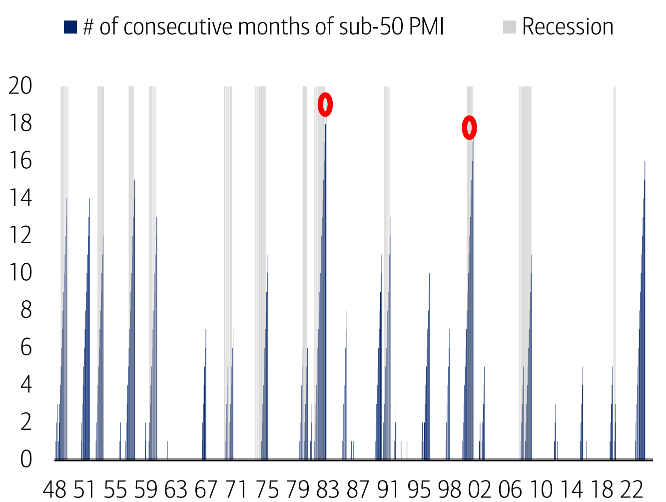
Exhibit 9: The third-longest manufacturing downturn in history (but without an economic recession)
# of consecutive months of sub-50 ISM PMI reading (1948-2/24)



Source: BofA US Equity & Quant Strategy, Bloomberg

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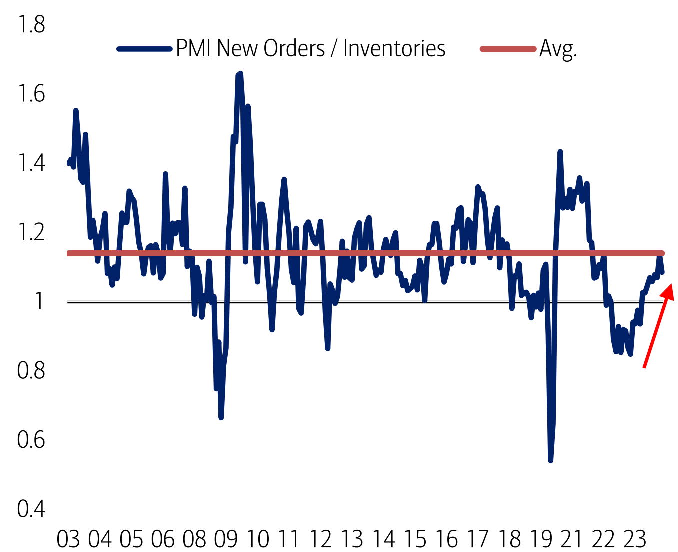
Exhibit 10: Inventory cycle is now back to normal
ISM PMI New Orders / Inventories (2003-2/24)



Source: BofA US Equity & Quant Strategy, Bloomberg

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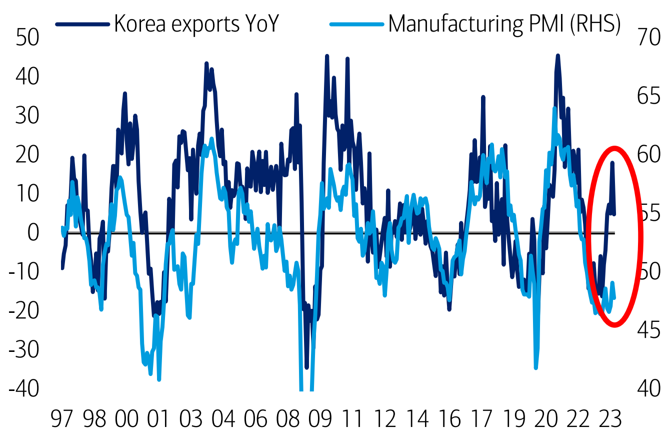
Exhibit 11: Korea exports soared, pointing to a manufacturing recovery
Korea exports YoY vs. ISM Manufacturing PMI (1997-2/24)



Source: BofA US Equity & Quant Strategy, Bloomberg
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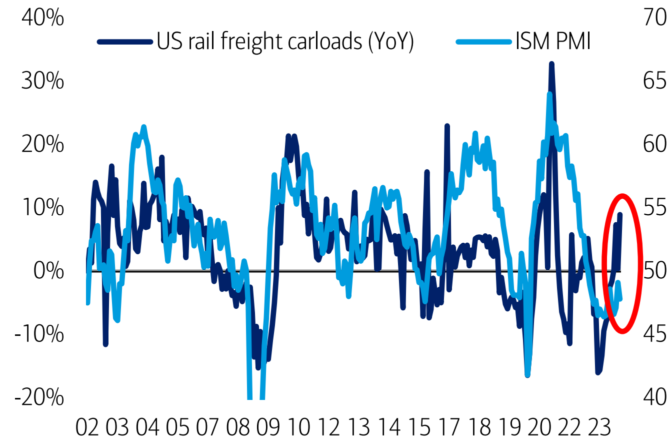
Exhibit 12: Rail freight volume also jumped
US rail freight carloads YoY vs. ISM Manufacturing PMI (2002-2/24)



Source: BofA US Equity & Quant Strategy, Bloomberg
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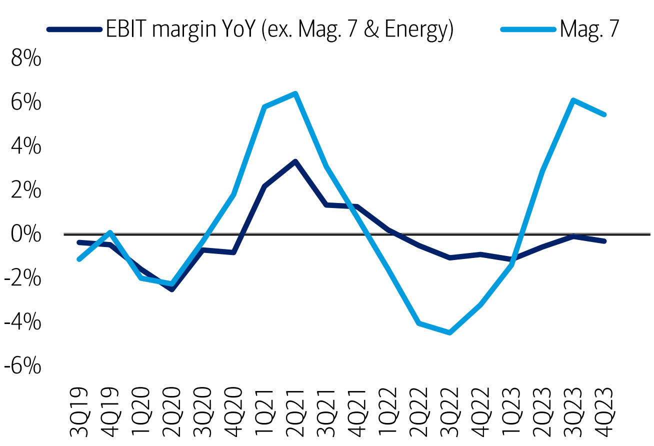
Tech cut costs, old economy is cutting costs

The other big headwind that caused an earnings recession in 2023 was bloated costs. Companies over-hired and overbuilt inventories during the earnings upcycle, which pressured margins when demand started to slow. But companies have aggressively cut costs aggressively, especially the Magnificent 7, whose margins recovered to highs. While Tech layoffs slowed substantially, layoff announcements picked up outside of Tech, which suggests that there is more cost cutting to be had, leading to better margins in 2024-25.

Exhibit 13: The Magnificent 7 recouped their margin loss by cutting costs
EBIT margin YoY ex. Energy & Financials (3Q19-4Q23)



Source: BofA US Equity & Quant Strategy, FactSet
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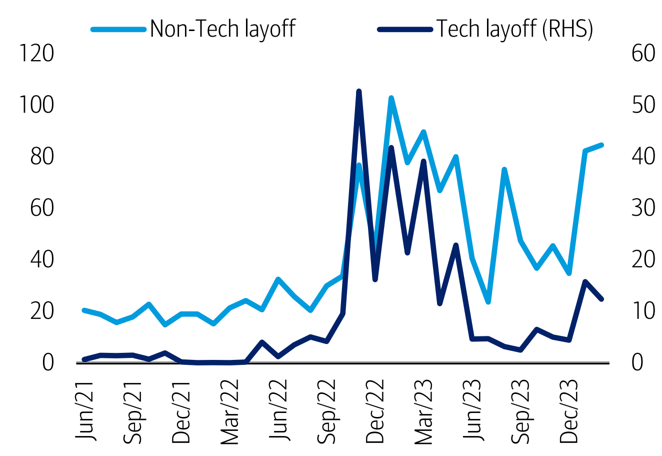
Exhibit 14: Layoffs remain high outside the Tech sector
Challenger US job cut announcement (6/21-2/24; ,000)



Source: BofA US Equity & Quant Strategy, Bloomberg
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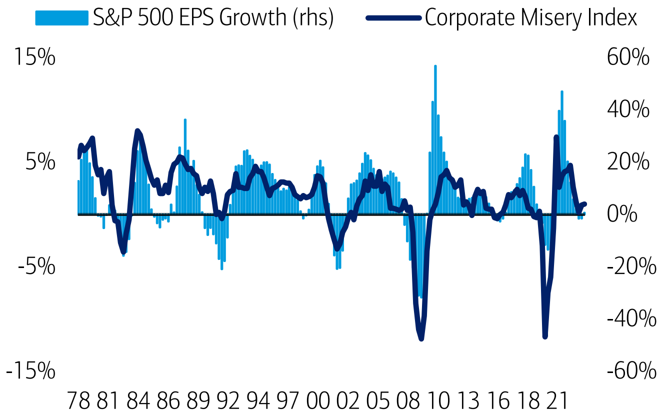
Macro indicator also suggests a better environment ahead

Our Corporate Misery Indicator, a macro gauge of the profits environment, improved for the second straight quarter, driven by better demand (Coincident Indicators), stronger pricing (CPI) and slowing wages (Avg. Hourly Earnings). This suggests improving macro conditions for corporate profits. While analysts are penciling in some margin improvement, we expect more upside surprises once demand starts to recover.

Exhibit 15: Our Corporate Misery indicator inflected higher in 4Q
BofA Corp. Misery Indicator (lower=more miserable) 4Q78-4Q23



Disclaimer: The indicator identified as BofA Corporate Misery Indicator above is intended to be an indicative metric only and may not be used for reference purposes or as a measure of performance for any financial instrument or contract, or otherwise relied upon by third parties for any other purpose, without the prior written consent of BofA Global Research. This indicator was not created to act as a benchmark. Note: see Appendix for full details/methodology.
Source: BofA US Equity & Quant Strategy, Conference Board, BLS

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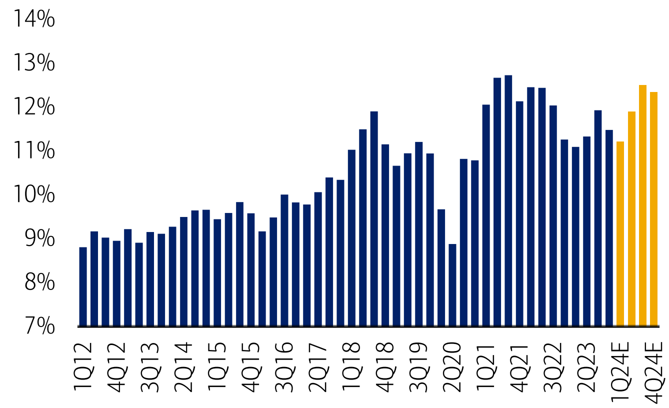
Exhibit 16: Analysts see margins strengthening from here, but not exceeding 2021's peak margins
S&P 500 quarterly net margins ex-Financials (2012-2024E)



Source: FactSet, BofA US Equity & Quant Strategy

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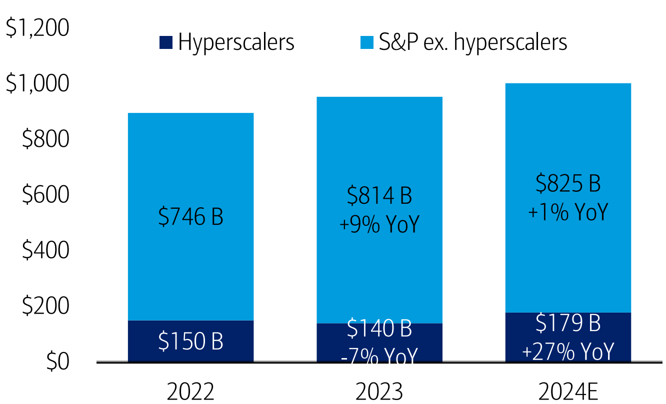
Virtuous cycle forming from AI investments

Hyperscalers (MSFT, AMZN, GOOGL, META) are expected to spend $180B on capex in 2024E, +27% YoY (Exhibit 17). The $38B YoY increase in capex represents nearly 80% of their expected increase in earnings YoY – i.e., they're entering a reinvestment cycle. History suggests companies in reinvestment cycles underperform (Exhibit 20), but we see a potential virtuous cycle forming from AI investments. Semis and networking are the most obvious beneficiaries (Exhibit 19), but increased power usage from AI and the physical build out of data centers will also lead to more demand for electrification, utilities, commodities, etc. (see AI impact to Industrials, Utilities, and Data Center REITs.

Exhibit 17: Hyperscalers are expected to drive most of capex growth for the S&P 500 in 2024
S&P 500 and hyperscalers (META, AMZN, GOOGL, META) capex



Source: BofA US Equity & Quant Strategy, FactSet

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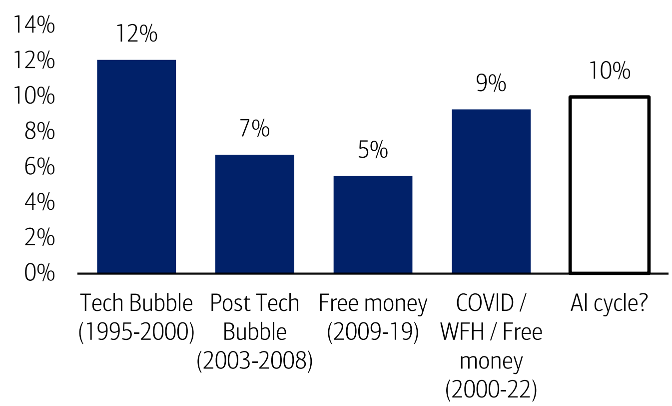
Exhibit 18: Tech investments have accelerated since COVID
Annualized growth in BEA private fixed investment on info processing equipment & software



Source: BofA US Equity & Quant Strategy, Bloomberg
*AI cycle's 10% growth represents 4Q23 SAAR QoQ

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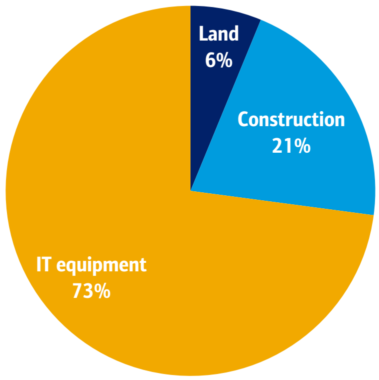
Exhibit 19: Who builds data centers?
% of data center capex by category



Source: US Chamber of Commerce

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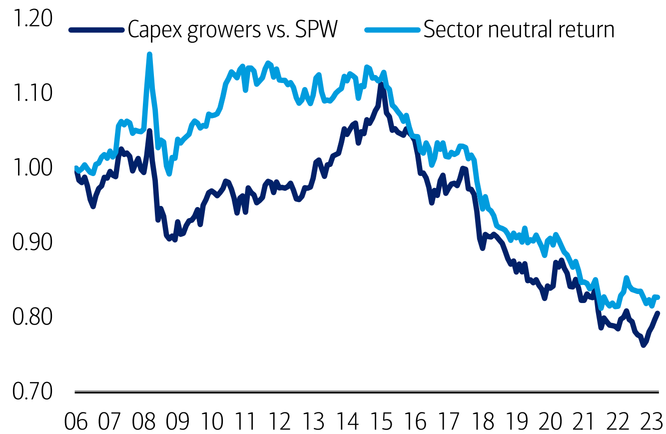
Exhibit 20: Capex growers have historically underperformed
Relative performance of top decile in expected capex YoY over the next 12 months vs. the equal-weighted S&P 500



Source: BofA US Equity & Quant Strategy, FactSet

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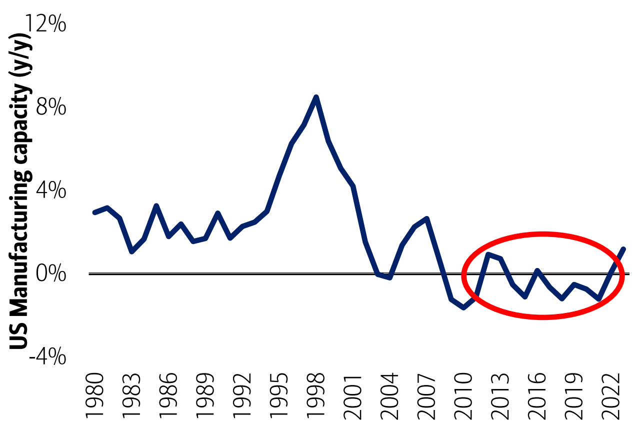
Welcome to a new productivity cycle

We see real evidence of an emerging productivity cycle, driven by the domestic investment cycle after 10+ years of underinvestment (plus AI). Re-shoring is also a big tailwind to improving productivity by building more efficient, new plants in the U.S. (or Mexico). Historically, productivity has increased two years after wage inflation as companies start to focus on improving efficiency via investing in capex.

And we are starting to see the fruition of investments made over the past two years, with the S&P 500's revenue per worker jumping to a record high after 15 years of no gains (Exhibit 26).

Exhibit 21: Domestic investment is picking up after 10 years of underinvestment
US manufacturing capacity YoY (1980-2023)



Source: Federal Reserve, BofA Global Research

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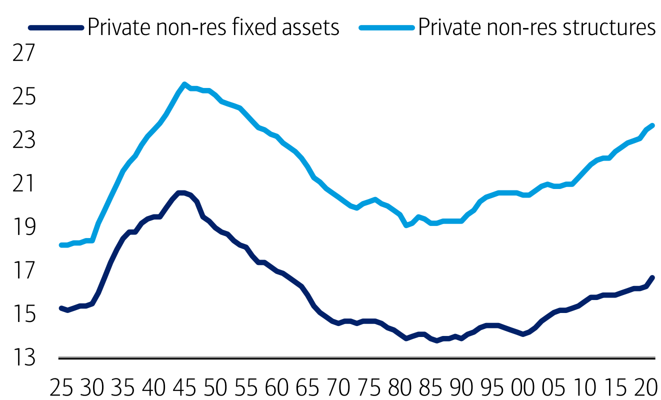
Exhibit 22: Stuff is old; we're due for a reinvestment cycle
Average age of private nonresidential fixed assets and structures (years; 1925-2021)



Source: BEA, BofA US Equity & US Quant Strategy

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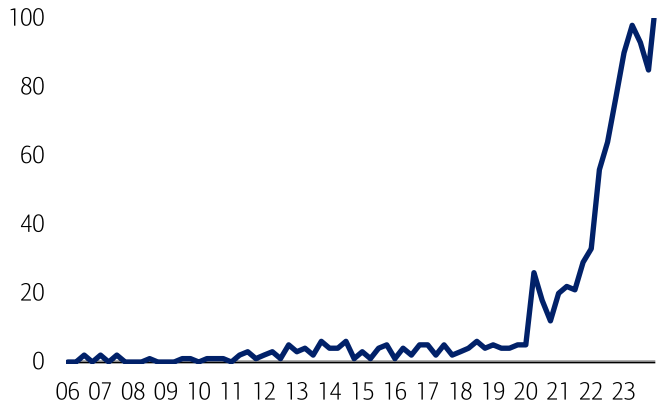
Exhibit 23: Mentions of re-shoring increased sharply over past year
Companies' mentions of re-/near-/on-shoring (100=max; 2006-2/24)



Source: AlphaSense, BofA Global Research

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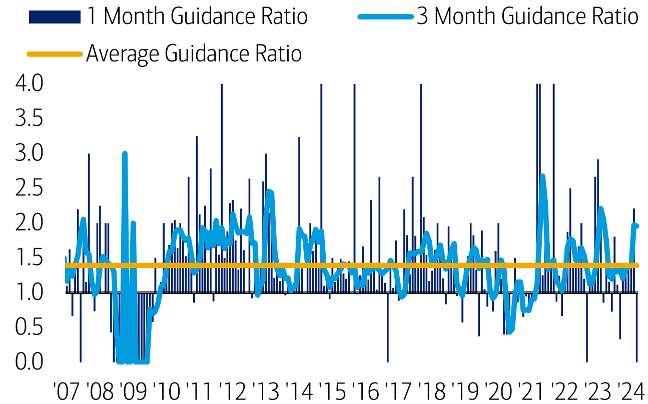
Exhibit 24: Twice as many companies are guiding above on capex than below
S&P 500 capex guidance ratio (# of above- vs. below-consensus capex guides)



Source: BofA US Equity & Quant Strategy, FactSet

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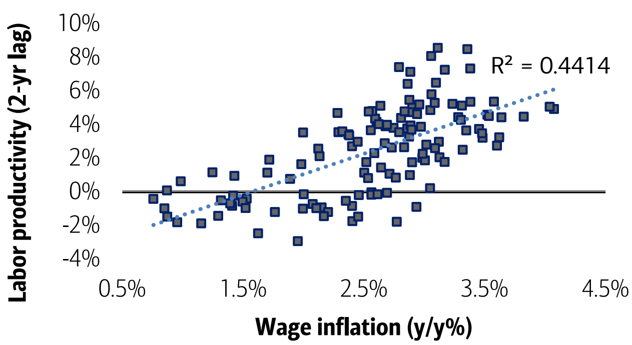
Exhibit 25: Wage inflation has driven labor productivity 2yrs out
US Manufacturing wage inflation and labor productivity (y/y % changes)



Source: Bureau of Labor Statistics, BofA Global Research
Note: Quarterly data of US manufacturing labor productivity versus average hourly earnings of production & nonsupervisory employees

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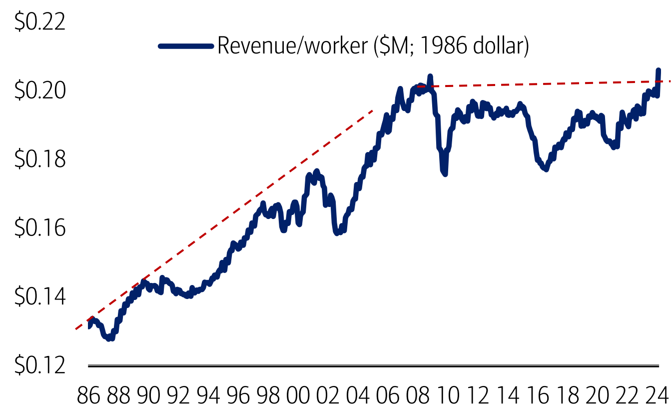
Exhibit 26: Labor productivity just jumped to a record high after 15 years of no gains
S&P 500 LTM revenue per employee ($M; 1985-2/24); adjusted for CPI



Source: BofA US Equity & Quant Strategy, FactSet, Bloomberg

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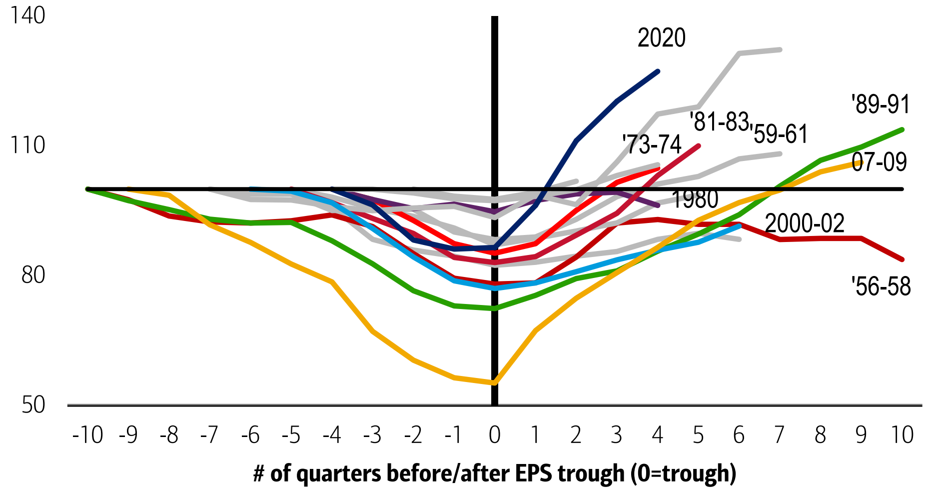
Earnings typically recover stronger than they fall

History suggests earnings typically recovery stronger than they fall (Exhibit 27), as downturns usually remove excess capacity, resulting in leaner cost structures and improved margin profiles. On average, S&P 500 TTM EPS exceeded prior peak levels by 5% after the same number of quarters into recovery as those into a downturn. This implies a projected TTM EPS of $233 by mid-2024, in line with our forecast.

Exhibit 27: Earnings typically recover stronger than they fall
S&P 500 TTM EPS before/after earnings troughs (same number of quarters leading to the trough and following the trough; 100=pre-recession peak; 1950-present)



Source: BofA US Equity & US Quant Strategy, FactSet, Haver Analytics

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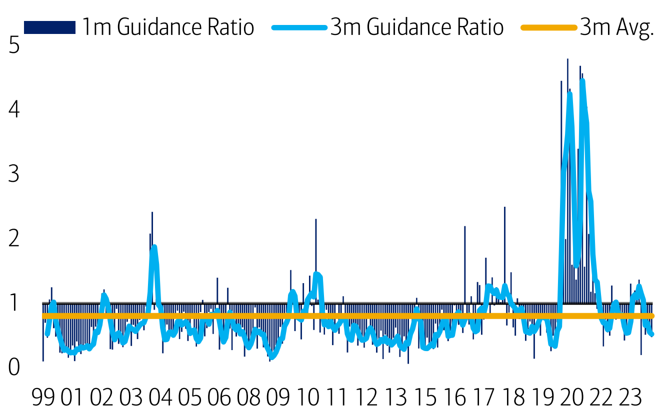
Guidance was weak, but likely due to conservatism

Our guidance ratio (# of above-consensus guides vs. below) fell to just 0.5x YTD, with twice as many companies guiding below consensus than above. While weaker than the historical average of 0.8x, Jan-Feb is seasonally the weakest period for guidance (Exhibit 29). Also, we see signs that weaker guides were due to conservatism rather than fundamental weakness. Our Corporate Sentiment Indicator, based on natural language processing (NLP) analysis, suggests that companies sounded more upbeat than ever during the 4Q earnings season. Improving Corporate Sentiment suggests continued earnings upcycle ahead (Exhibit 31).

Exhibit 28: Our guidance ratio is tracking at just 0.5x (i.e. twice as many below-consensus guide than above)
S&P 500 guidance ratio (# above vs. below consensus) – 1999-2/24



Source: BofA US Equity and Quantitative Strategy

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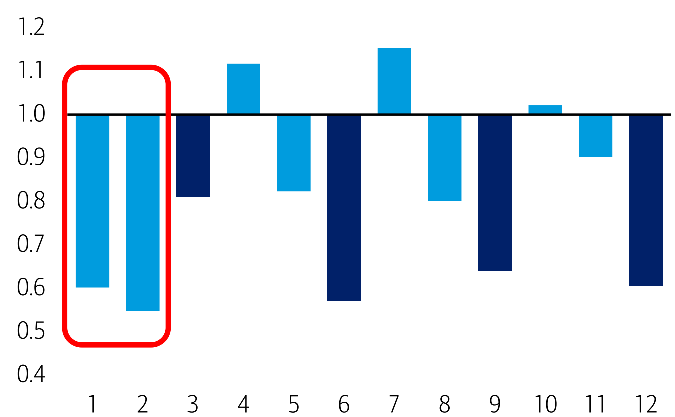
Exhibit 29: But Jan-Feb is seasonally the weakest period for guidance (light blue = earnings seasons)
Avg. 1-mo. guidance ratio by month (1999-2023)



Source: Bloomberg, BofA US Equity & Quant Strategy

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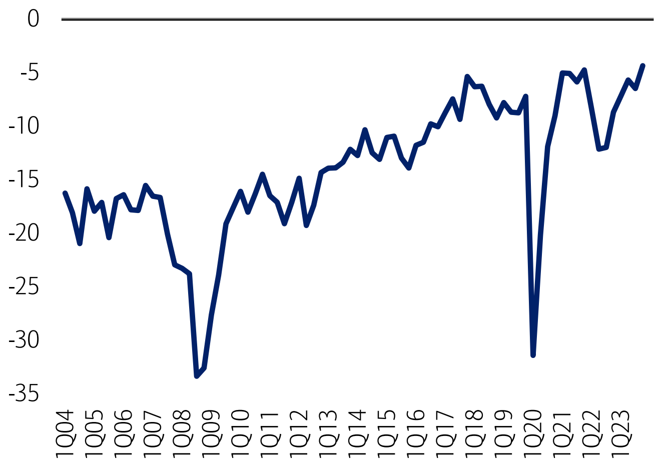
Exhibit 30: Despite weaker guidance, corporate sentiment improved to a record high, suggesting conservatism in guidance
Avg. negative sentiment score for S&P 500 companies (2004-4Q23)



Source: BofA Global Research, FactSet

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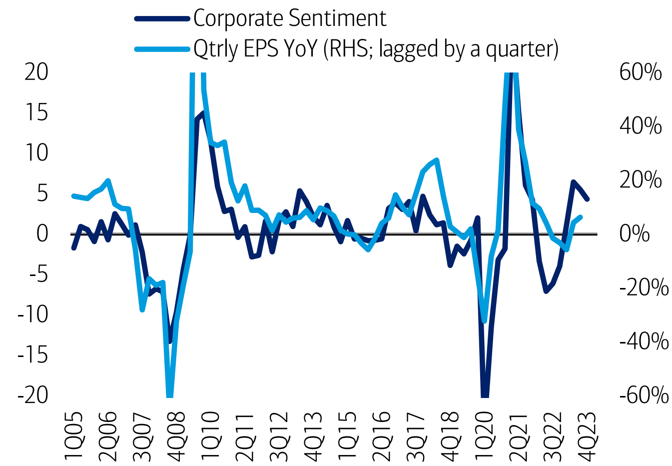
Exhibit 31: Improving corporate sentiment suggests continued upcycle in earnings
S&P 500 avg. negative sentiment score YoY vs. quarterly EPS YoY with a quarter lag (r-sq=48%; 1Q05-4Q23)



Source: BofA Global Research, FactSet

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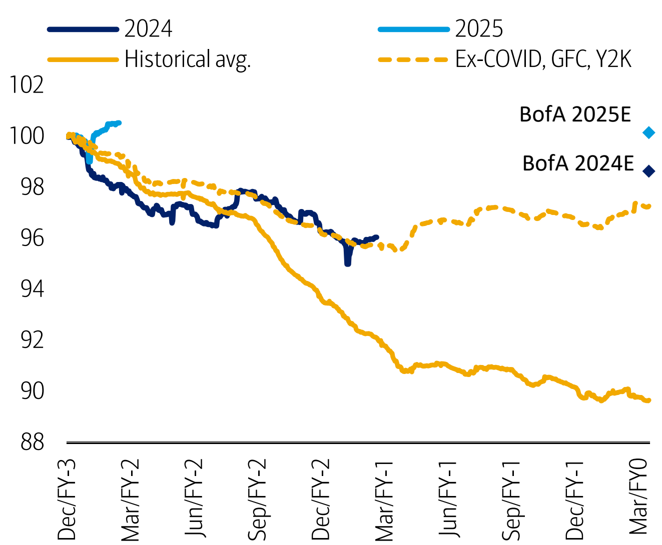
Analysts are usually too optimistic, but only in recession years

Historically, FY2 EPS were cut by 10% vs. initial forecasts as analysts typically start the year optimistically. However, excluding recession years (Tech Bubble, Global Financial Crisis, and COVID), FY2 EPS were only cut by 3%. Also, compared to consensus estimates as of March a year before (i.e., where we stand today for 2024 EPS), EPS actually came in 2% higher.

Exhibit 32: Excluding recession years, estimates have historically held up
S&P 500 historical FY2 EPS revisions vs. 2024-25 consensus EPS (2024-25 as of 3/9/24)



Source: BofA US Equity & Quant Strategy, FactSet; Note: historical average based on 2001-2022

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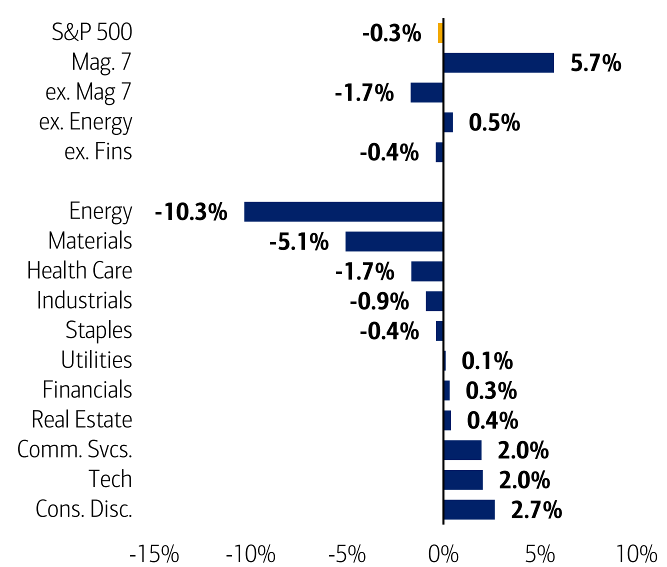
Exhibit 33: 2024 consensus EPS has been largely unchanged YTD
S&P 500 2024 consensus EPS revision YTD (as of 3/9/24)



Source: BofA US Equity & Quant Strategy, FactSet

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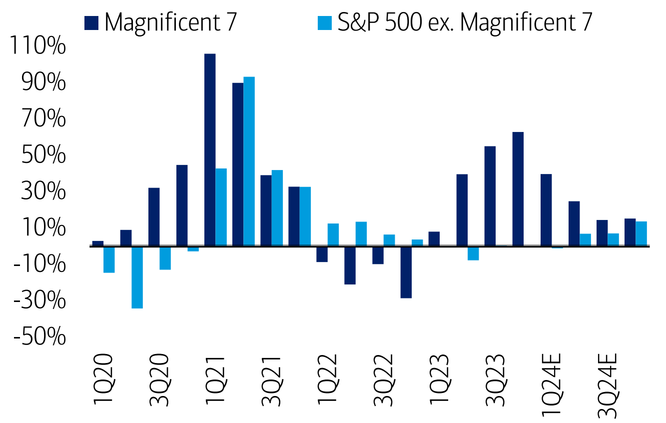
Converging growth between the Mag. 7 vs. the other 493

The Magnificent 7 continued to drive the S&P 500's EPS recovery in 4Q, growing 60%+ YoY, while earnings for the other 493 constituents were flat. But going forward, we expect earnings to decelerate for the Mag. 7, but accelerate for the other 493, with the growth differential essentially merging by 4Q24. Given the high correlation between Tech's outperformance in stocks vs. earnings, we expect the narrowing growth differential to be a catalyst for the market to broaden out.

Exhibit 34: We expect growth differentials to narrow between the Magnificent 7 vs. the other 493

Magnificent 7 vs. the other 493 quarterly EPS YoY



Source: BofA US Equity & Quant Strategy, FactSet

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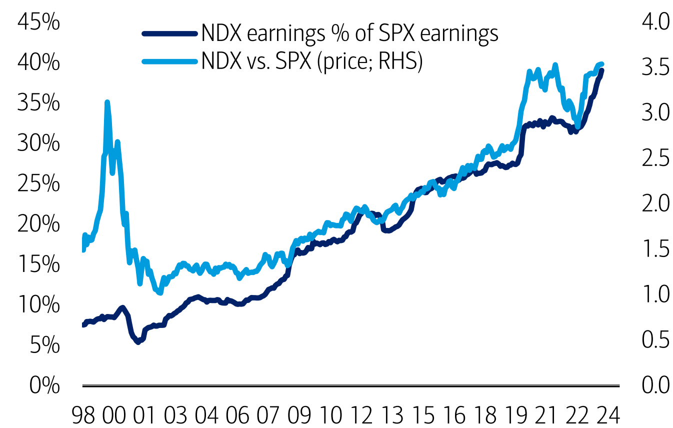
Exhibit 35: Tech's outperformance has been highly correlated to its earnings vs. S&P 500 since the Tech Bubble. Narrowing growth differentials should lead to the market broadening out

Nasdaq 100 vs. S&P 500 – earnings and performance (1998-2/24)



Source: BofA US Equity & Quant Strategy, FactSet

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