

MARKET MINUTE

WITH MCGAREL



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¹Capital IQ.

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Why do we believe value stocks will outperform growth stocks over the next several years? For the same exact reason that growth stocks outperformed value stocks in 2020 and 2021. Earnings growth!

In 2020, stocks in the S&P 500 Growth Index saw earnings increase 9.7% while stocks in the S&P 500 Value Index saw earnings decline 25.6%. Last year growth stocks again increased earnings at a faster pace than value stocks, 58.4% versus 49.3%, respectively. Is it any wonder that the S&P 500 Growth Index returned 76.16% and the S&P 500 Value Index only increased 26.54% over the last two calendar years? ¹

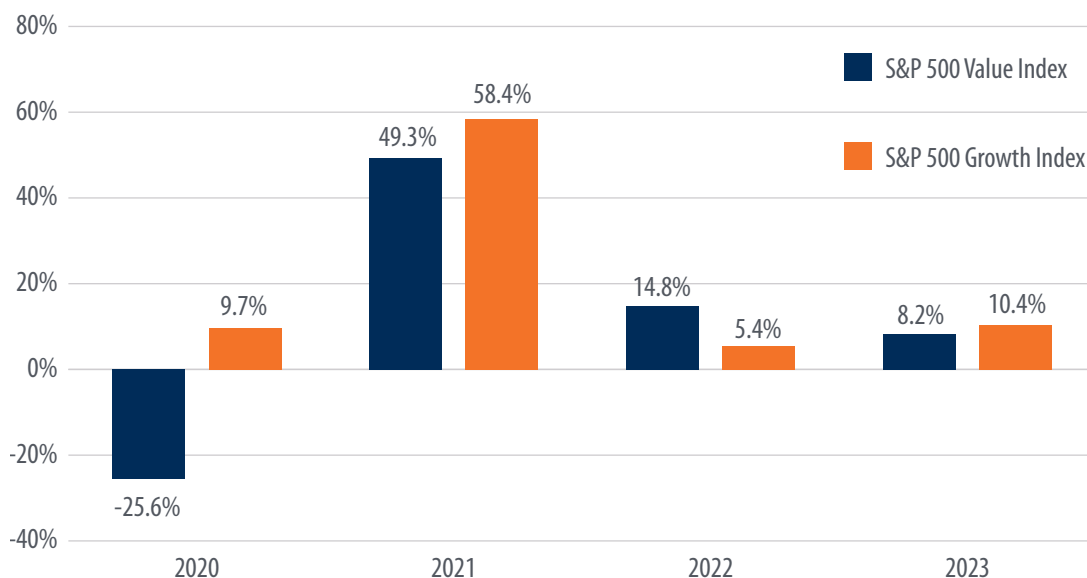
For all the inputs that investors analyze to determine where to invest, whether it be fiscal and monetary policy, taxes, regulation, geopolitical events, secular trends, etc., at the end of the day, stocks follow earnings.

If we look at earnings growth expectations for 2022 and 2023, the chart below tells a remarkably different story than the previous two years. This year the S&P 500 Value Index is expected to grow earnings 14.8%, much faster than the S&P 500 Growth Index earnings expectations of 5.4%. For 2023, the S&P 500 Growth Index is only expected to modestly outgrow the S&P 500 Value Index, 10.4% to 8.2%.

Additionally, when we consider that earnings growth going forward is forecast to be much slower than last year for the entire market, valuation becomes more important to investors. Per Bloomberg, the S&P 500 Growth Index currently trades at 23.7 times earnings while the S&P 500 Value Index trades at 18.3 times this year's earnings. Looking at the forward P/E valuations of the S&P 500 Pure Growth Index and S&P 500 Pure Value Index, the differences are even more stark with growth trading at 25.3x versus 12.4x for value.¹

So we are left with faster forecasted earnings growth over the next two years for value stocks which also trade at a nice discount to growth stocks. We favor value stocks in this environment.

Expected Earnings Growth Rates: S&P 500 Value Index and S&P 500 Growth Index



Source: Bloomberg. As of 5/31/22. Earnings growth rates are based on aggregate sell-side estimates. For illustrative purposes only and not indicative of any investment. The **S&P 500 Index** is an unmanaged index of 500 companies used to measure large-cap U.S. stock market performance. The **S&P 500 Growth Index** contains those securities with growth characteristics from the S&P 500 Index. The **S&P 500 Value Index** contains those securities with value characteristics from the S&P 500 Index. Investors cannot invest directly in an index. **Earnings per share (EPS)** is calculated as a company's profit divided by the outstanding shares of its common stock. The resulting number serves as an indicator of a company's profitability. **EPS growth** illustrates the growth of earnings per share over time. There is no assurance any forecasts will be achieved.