



All Cap Index & Sectors: 1Q22's Soaring Economic Earnings Aren't Sustainable

[Economic earnings](#) increased year-over-year (YoY) for all but two sectors through the trailing-twelve-months (TTM) ended 1Q22 for the NC 2000¹, our All Cap Index.

This report analyzes the economic earnings² (which adjust for [unusual items](#) on both the income statement and balance sheet) and GAAP earnings of the NC 2000 and its sectors. Economic earnings provide a more accurate picture of the true underlying cash flows of a business than GAAP earnings. Reports on the drivers of economic earnings – return on invested capital ([ROIC](#)), net operating profit after tax ([NOPAT](#)) margin, [invested capital turns](#), and the weighted average cost of capital ([WACC](#)) for the NC 2000 and its sectors are [here](#).

This report leverages our cutting-edge [Robo-Analyst technology](#) to deliver [proven-superior](#)³ fundamental research and support more cost-effective fulfillment of the [fiduciary duty of care](#).

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Economic Earnings Nearly Doubled in 1Q22

Figure 1 shows economic earnings for the NC 2000 rose from \$563.4 billion in 1Q21 to \$1.0 trillion in 1Q22, while GAAP Earnings rose from \$1.3 trillion to \$2.1 trillion over the same time. Economic and GAAP earnings are only slightly below calendar 2021 levels – the highest since 1998, which is the earliest our analysis is available.

Figure 1: NC 2000 Economic Earnings Vs. GAAP: 1998 – 1Q22



Sources: New Constructs, LLC and company filings.

Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the NC 2000 constituents were available.

¹ The NC 2000 consists of the largest 2000 U.S. companies by market cap in our coverage. Constituents are updated on a quarterly basis (March 31, June 30, September 30, and December 31). We exclude companies that report under IFRS and non-U.S. ADR companies.

² This report is based on the latest audited financial data available, which is the 1Q22 10-Q in most cases. Price data as of 5/16/22.

³ Our research utilizes our more of reliable fundamental data, as proven in [Core Earnings: New Data & Evidence](#), written by professors at Harvard Business School (HBS) & MIT Sloan and published in [The Journal of Financial Economics](#).



However, the NC 2000's soaring economic earnings are likely to reverse trend soon, as we detail in [All Cap Index & Sectors: Inflation Inflates ROICs for 1Q22](#). Indeed, a major headwind facing economic earnings is a rising WACC, which in the TTM ended 1Q22 added \$104.1 billion to the cost of capital. The start of rapid inflation artificially boosts GAAP earnings as profits on current sales are calculated using historic inventory costs. Once inflation cools, the process is reversed, and GAAP earnings become artificially depressed. However, investors can protect themselves from such false signals by utilizing economic earnings, which accounts for expected inflation as reflected in the firm's WACC.

Ranking the Sectors by GAAP Vs. Economic Earnings Change

Figure 2 compares the YoY change in economic earnings and GAAP earnings from 1Q21 to 1Q22⁴ for the NC 2000 and all eleven NC 2000 sectors.

Figure 2: 1Q22 Economic Earnings & GAAP Earnings YoY Change (\$ Billions)

Sector	GAAP Earnings YoY Change	Economic Earnings YoY Change	Difference
Consumer Cyclical	\$121.4	\$50.4	\$71.0
Financials	\$71.5	\$10.5	\$61.0
Technology	\$127.5	\$86.1	\$41.4
Industrials	\$95.1	\$54.9	\$40.2
Energy	\$192.6	\$158.0	\$34.6
Consumer Non-cyclicals	\$30.4	\$3.1	\$27.3
Telecom Services	\$27.8	\$2.9	\$24.9
Healthcare	\$74.0	\$54.5	\$19.6
Real Estate ⁵	\$14.3	(\$1.3)	\$15.6
Utilities	\$8.7	(\$6.6)	\$15.3
Basic Materials	\$51.6	\$51.9	(\$0.3)
NC 2000	\$819.5	\$464.4	\$355.2

Sources: New Constructs, LLC and company filings.

Our economic earnings analysis is based on aggregated TTM data for the sector constituents.

While all sectors saw a YoY rise in GAAP earnings, economic earnings for the Real Estate and Basic Materials sectors fell in 1Q22.

The Energy sector saw the largest YoY improvement, \$158.0 billion, in economic earnings, which rose from -\$112.1 billion in 1Q21 to \$45.8 billion in 1Q22.

The Technology sector generates the most economic earnings of any sector and grew economic earnings by 30% YoY in 1Q22. On the flip side, the Real Estate sector has the lowest economic earnings and saw a \$1.3 billion YoY decline in economic earnings in 1Q22.

Details on the 11 NC 2000 Sectors

Figures 3 through 13 below compare the economic earnings and GAAP earnings trends for every NC 2000 sector since 1998.

⁴ May 16, 2022, is earliest date for which all the calendar 1Q22 10-Qs for the NC 2000 constituents were available.

⁵ We use Funds from Operations (FFO) for the Real Estate sector rather than GAAP Earnings.

**Basic Materials**

Figure 3 shows economic earnings for the Basic Materials sector, at \$59.3 billion, rose 699% YoY in 1Q22, while GAAP earnings, at \$92.5 billion, rose 126% over the same time.

Figure 3: Basic Materials Economic Earnings Vs. GAAP: 1998 – 1Q22

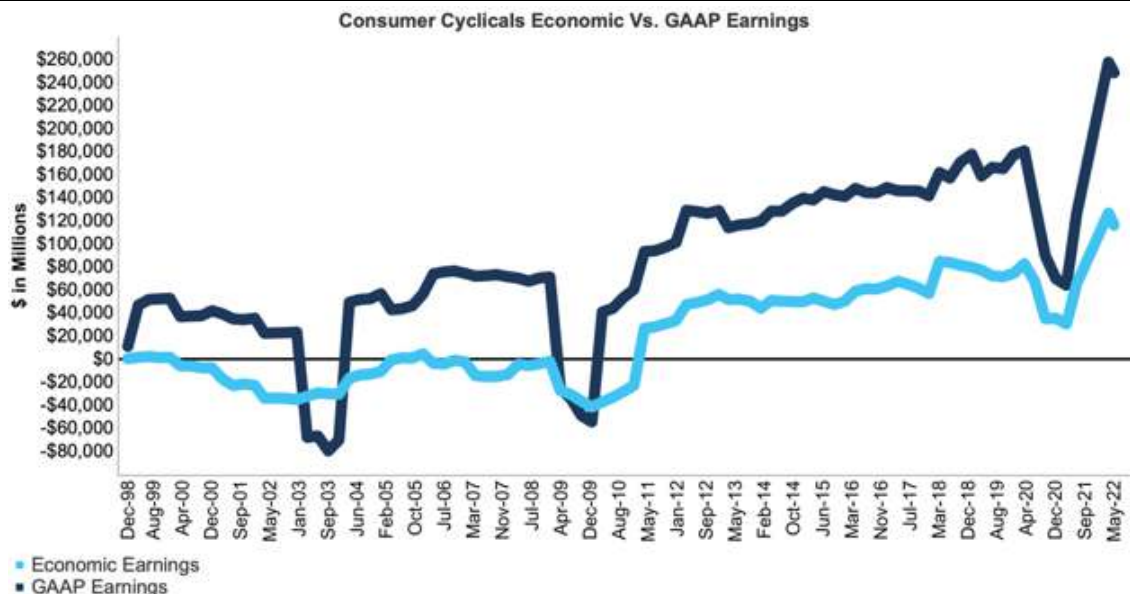
Sources: New Constructs, LLC and company filings.

Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

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Consumer Cyclical

Figure 4 shows economic earnings for the Consumer Cyclical sector, at \$116 billion, rose 77% YoY in 1Q22, while GAAP earnings, at \$248.3 billion, rose 96% over the same time.

Figure 4: Consumer Cyclical Economic Earnings Vs. GAAP: 1998 – 1Q22

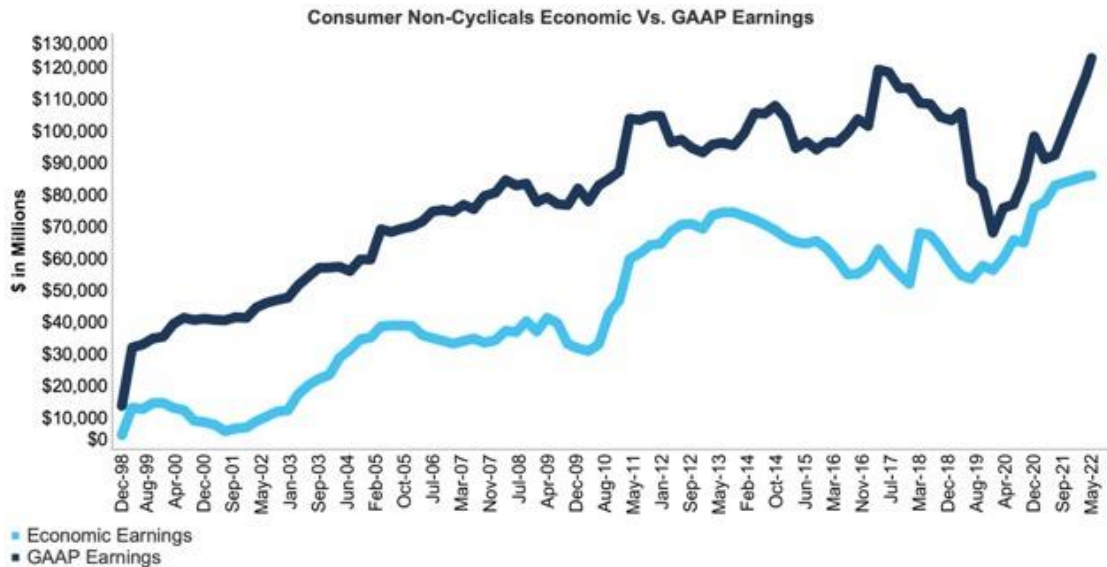
Sources: New Constructs, LLC and company filings.

Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

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**Consumer Non-Cyclicals**

Figure 5 shows economic earnings for the Consumer Non-Cyclicals sector, at \$86.2 billion, rose 4% YoY in 1Q22, while GAAP earnings, at \$123.0 billion, rose 33% over the same time.

Figure 5: Consumer Non-Cyclicals Economic Earnings Vs. GAAP: 1998 – 1Q22

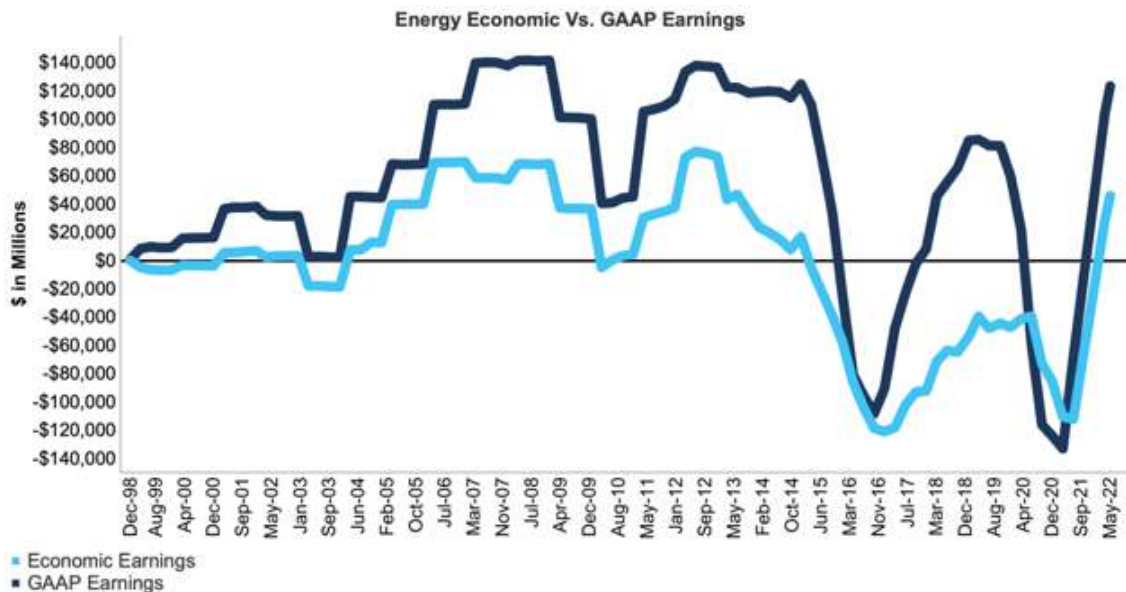
Sources: New Constructs, LLC and company filings.

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Energy

Figure 6 shows economic earnings for the Energy sector rose from -\$112.1 billion in 1Q21 to \$45.8 billion in 1Q22, while GAAP earnings rose from -\$69.2 billion to \$123.4 billion over the same time.

Figure 6: Energy Economic Earnings Vs. GAAP: 1998 – 1Q22

Sources: New Constructs, LLC and company filings.

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**Financials**

Figure 7 shows economic earnings for the Financials sector, at \$125.81 billion, rose 9% YoY in 1Q22, while GAAP earnings, at \$481.4 billion rose 17% over the same time.

Figure 7: Financials Economic Earnings Vs. GAAP: 1998 – 1Q22

Sources: New Constructs, LLC and company filings.

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Healthcare

Figure 8 shows economic earnings for the Healthcare sector, at \$158.5 billion, rose 52% YoY in 1Q22, while GAAP earnings, at \$213.3 billion, rose 53% over the same time.

Figure 8: Healthcare Economic Earnings Vs. GAAP: 1998 – 1Q22

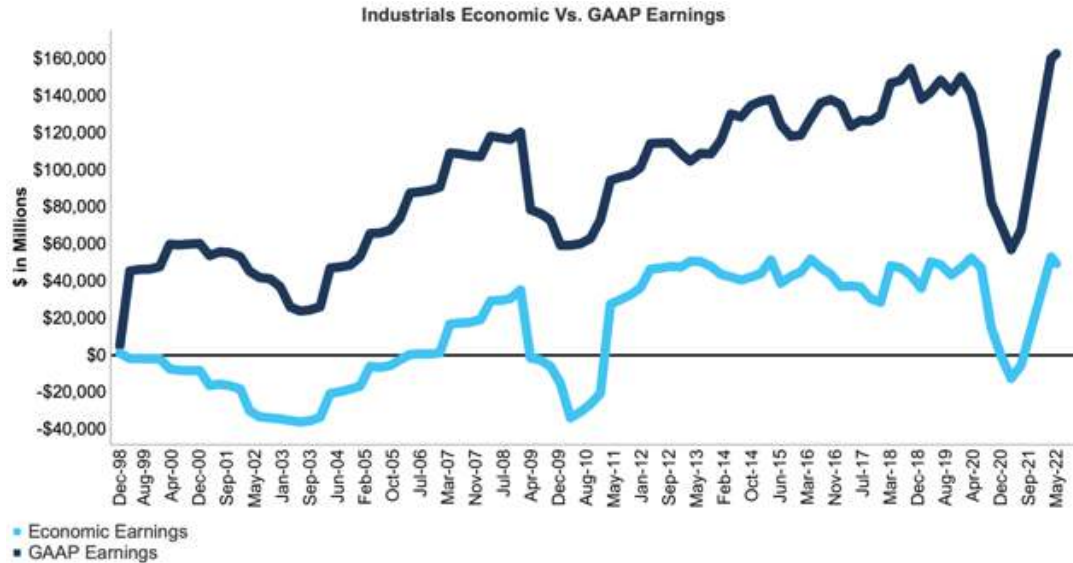
Sources: New Constructs, LLC and company filings.

Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

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**Industrials**

Figure 9 shows economic earnings for the Industrials sector rose from -\$5.5 billion in 1Q21 to \$49.4 billion in 1Q22, while GAAP earnings rose from \$67.7 billion to \$162.8 billion over the same time.

Figure 9: Industrials Economic Earnings Vs. GAAP: 1998 – 1Q22

Sources: New Constructs, LLC and company filings.

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Real Estate

Figure 10 shows economic earnings for the Real Estate sector fell from -\$7.1 billion in 1Q21 to -\$8.4 billion in 1Q22, while funds from operations rose from \$46.1 billion to \$60.4 billion over the same time. Funds from operations add back depreciation and amortization, which can materially impact reported results.

Figure 10: Real Estate Economic Earnings Vs. FFO: 1998 – 1Q22

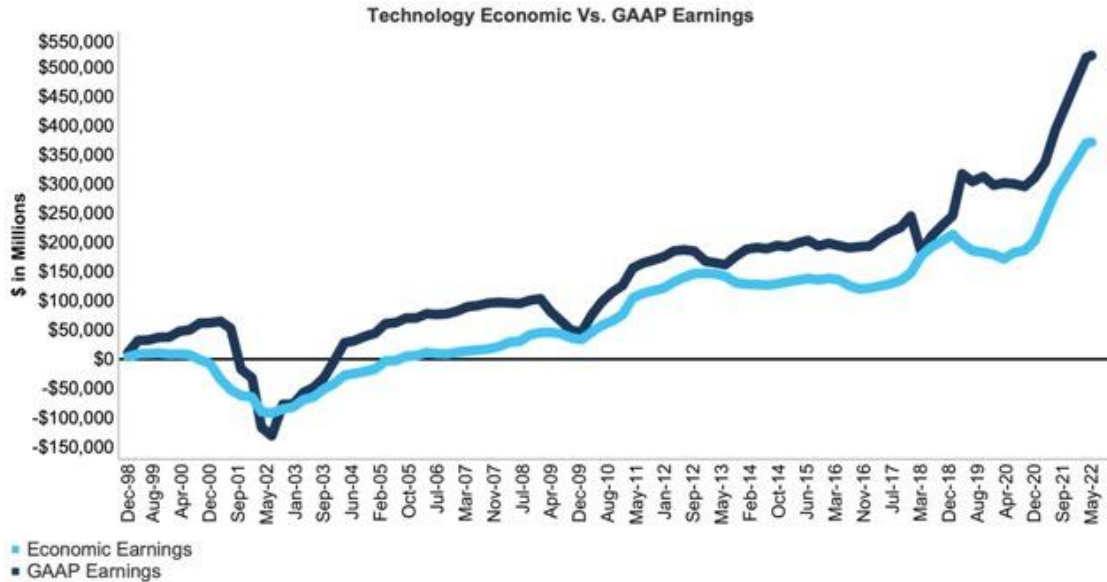
Sources: New Constructs, LLC and company filings.

Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

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**Technology**

Figure 11 shows economic earnings for the Technology sector, at \$371.9 billion, rose 30% YoY in 1Q22, while GAAP earnings, at \$520.4 billion, rose 32% over the same time.

Figure 11: Technology Economic Earnings Vs. GAAP: 1998 – 1Q22

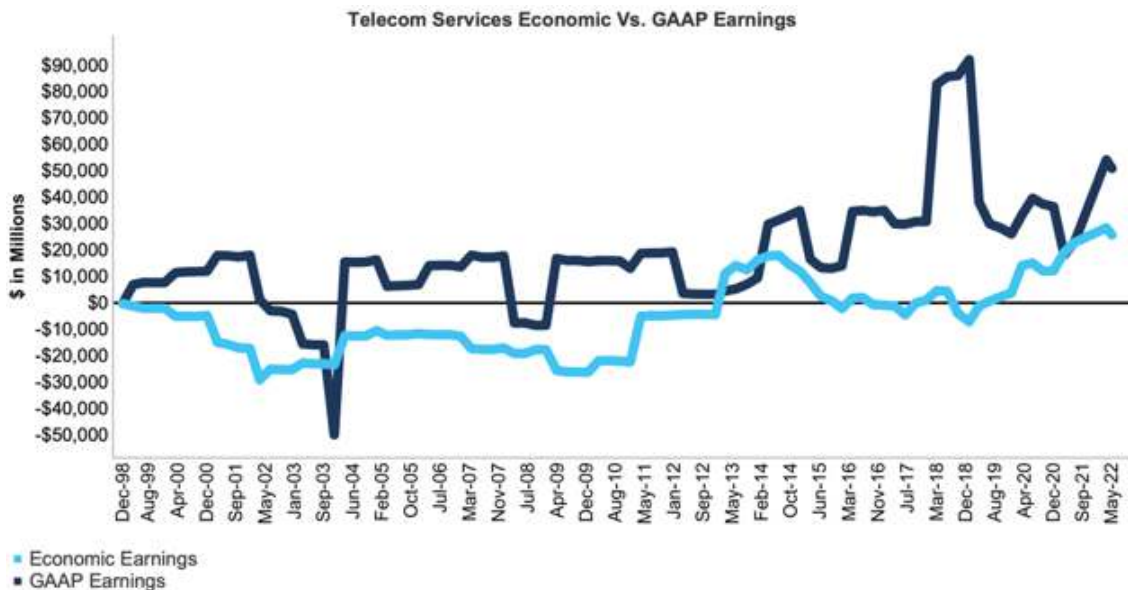
Sources: New Constructs, LLC and company filings.

Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

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Telecom Services

Figure 12 shows economic earnings for the Telecom Services sector, at \$25.8 billion, rose 12% YoY in 1Q22, while GAAP earnings, at \$51.0 billion, rose 119% over the same time.

Figure 12: Telecom Services Economic Earnings Vs. GAAP: 1998 – 1Q22

Sources: New Constructs, LLC and company filings.

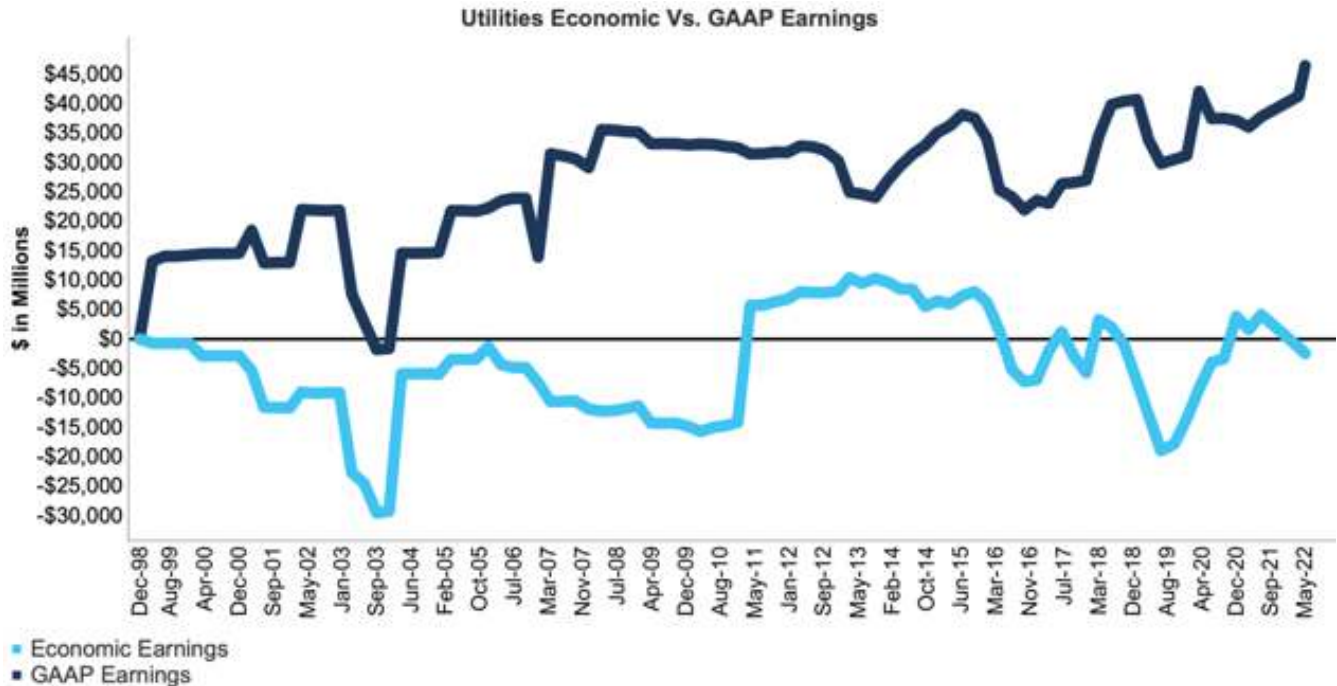
Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

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**Utilities**

Figure 13 shows economic earnings for the Utilities sector fell from \$4.1 billion in 1Q21 to -\$2.5 billion in 1Q22, while GAAP earnings rose from \$37.7 billion to \$46.4 billion over the same time.

Figure 13: Utilities Economic Earnings Vs. GAAP: 1998 – 1Q22



Sources: New Constructs, LLC and company filings.

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This article originally published on [June 3, 2022](#).

Disclosure: David Trainer, Kyle Guske II, and Matt Shuler receive no compensation to write about any specific stock, style, or theme.

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Appendix: Calculation Methodology

We derive the economic earnings and GAAP earnings metrics above by summing the Trailing Twelve-Month individual NC 2000 constituent values for economic earnings and GAAP earnings in each sector for each measurement period. We call this approach the “Aggregate” methodology.

The Aggregate methodology provides a straightforward look at the entire sector, regardless of market cap or index weighting and matches how S&P Global (SPGI) calculates metrics for the S&P 500.



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Key quotes from the paper:

- “[New Constructs’] *Total Adjustments* differs significantly from the items identified and excluded from Compustat’s adjusted earnings measures. For example... 50% to 70% of the variation in *Total Adjustments* is not explained by *S&P Global’s (SPGI) Adjustments* individually.” – pp. 14, 1st para.
- “A final source of differences [between New Constructs’ and S&P Global’s data] is due to data collection oversights...we identified cases where Compustat did not collect information relating to firms’ income that is useful in assessing core earnings.” – pp. 16, 2nd para.

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Key quotes from the paper:

- “...an accurate calculation of ROIC requires more diligence than often occurs in some of the common, off-the-shelf ROIC calculations. Only by scouring the footnotes and the MD&A [as New Constructs does] can investors get an accurate calculation of ROIC.” – pp. 8, 5th para.
- “The majority of the difference...comes from New Constructs’ machine learning approach, which leverages technology to calculate ROIC by applying accounting adjustments that may be buried deeply in the footnotes across thousands of companies.” – pp. 4, 2nd para.

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Key quotes from the paper:

- “the portfolios formed following the buy recommendations of Robo-Analysts earn abnormal returns that are statistically and economically significant.” – pp. 6, 3rd para.
- “Our results ultimately suggest that Robo-Analysts are a valuable, alternative information intermediary to traditional sell-side analysts.” – pp. 20, 3rd para.

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