



## S&P 500 Economic Earnings Set Records, but WACC Is a Drag

[Economic earnings](#) increased year-over-year (YoY) for all but one sector through the trailing-twelve-months (TTM) ended 1Q22.

This report analyzes the economic earnings<sup>1</sup> (which adjust for [unusual items](#) on both the income statement and balance sheet) and GAAP earnings for the S&P 500 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 S&P 500 and its sectors are [here](#).

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### Economic Earnings Rise to New Highs in 1Q22

Figure 1 shows economic earnings for the S&P 500 rose from \$537.5 billion in 1Q21 to \$933.7 billion in 1Q22, while GAAP Earnings rose from \$1.2 trillion to \$1.8 trillion over the same time. Economic and GAAP earnings are at their highest levels since 2004, which is the earliest our analysis is available.

**Figure 1: S&P 500 Economic Earnings Vs. GAAP: 2004 – 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 S&P 500 constituents were available.

However, the S&P 500's soaring economic earnings are likely to reverse trend soon, as we detail in [S&P 500 & Sectors: ROIC Hits New Peak, but Can It Last?](#). Indeed, a major headwind facing economic earnings is a rising

<sup>1</sup> 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.

<sup>2</sup> 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](#).



WACC, which in the first quarter added \$84.5 billion to the cost of capital. Inflation tends only to boost GAAP earnings, and investors can protect themselves from such false signals by paying closer attention to economic earnings. This measure 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 1Q22<sup>3</sup> for the S&P 500 and all eleven S&P 500 sectors.

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

Sector	GAAP Earnings YoY Change	Economic Earnings YoY Change	Difference
Financials	\$59.6	\$17.5	\$42.1
Consumer Cyclical	\$63.8	\$24.8	\$39.1
Technology	\$122.5	\$93.5	\$28.9
Industrials	\$71.2	\$43.1	\$28.1
Energy	\$163.4	\$138.6	\$24.8
Healthcare	\$78.9	\$54.2	\$24.6
Telecom Services	\$26.5	\$3.6	\$22.9
Consumer Non-cyclicals	\$24.4	\$1.7	\$22.8
Utilities	\$2.8	(\$8.3)	\$11.1
Real Estate <sup>4</sup>	\$9.7	\$1.6	\$8.1
Basic Materials	\$25.0	\$26.0	(\$1.0)
<b>S&amp;P 500</b>	<b>\$647.7</b>	<b>\$396.2</b>	<b>\$251.5</b>

Sources: New Constructs, LLC and company filings.

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

The Energy sector saw the largest YoY improvement, \$138.6 billion, in economic earnings, which rose from - \$93.1 billion in 1Q21 to \$45.6 billion in 1Q22.

The Technology sector generates the most economic earnings of any sector and grew economic earnings by 31% YoY in 1Q22. On the flip side, the Utilities sector has the lowest economic earnings and was the only sector to see a YoY decline in economic earnings in 1Q22.

### Details on the 11 S&P 500 Sectors

Figures 3 through 13 below compare the economic earnings and GAAP earnings trends for every S&P 500 sector since 2004.

<sup>3</sup> May 16, 2022, is earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.

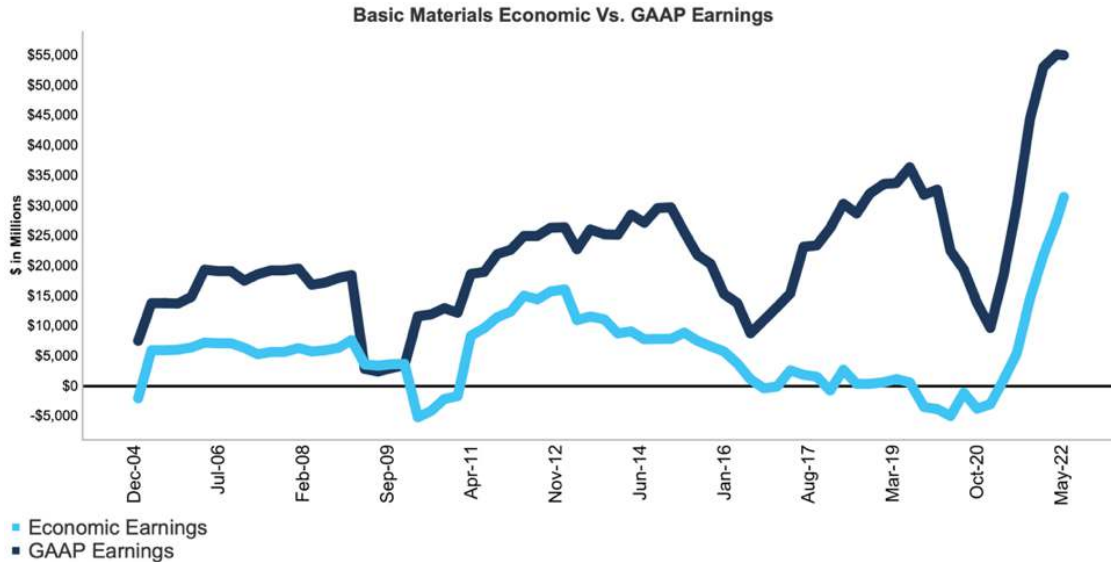
<sup>4</sup> We use Funds from Operations (FFO) for the Real Estate sector rather than GAAP Earnings.



### Basic Materials

Figure 3 shows economic earnings for the Basic Materials sector, at \$31.4 billion, rose 476% YoY in 1Q22, while GAAP earnings, at \$55 billion, rose 83% over the same time.

**Figure 3: Basic Materials Economic Earnings Vs. GAAP: 2004 – 1Q22**

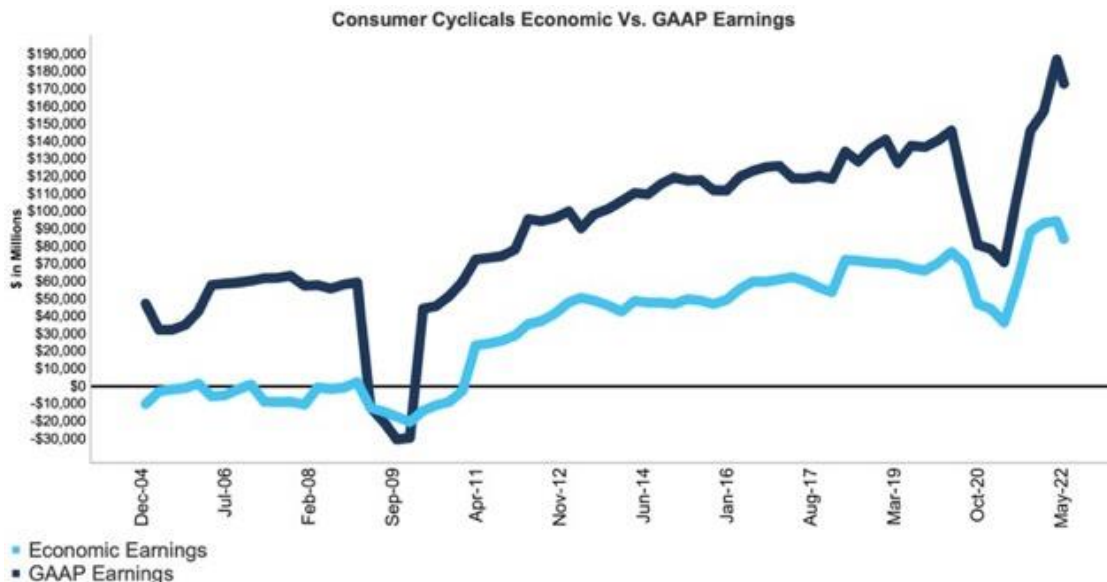


Sources: New Constructs, LLC and company filings. Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period. The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.

### Consumer Cyclical

Figure 4 shows economic earnings for the Consumer Cyclical sector, at \$84.2 billion, rose 42% YoY in 1Q22, while GAAP earnings, at \$173.0 billion, rose 58% over the same time.

**Figure 4: Consumer Cyclical Economic Earnings Vs. GAAP: 2004 – 1Q22**



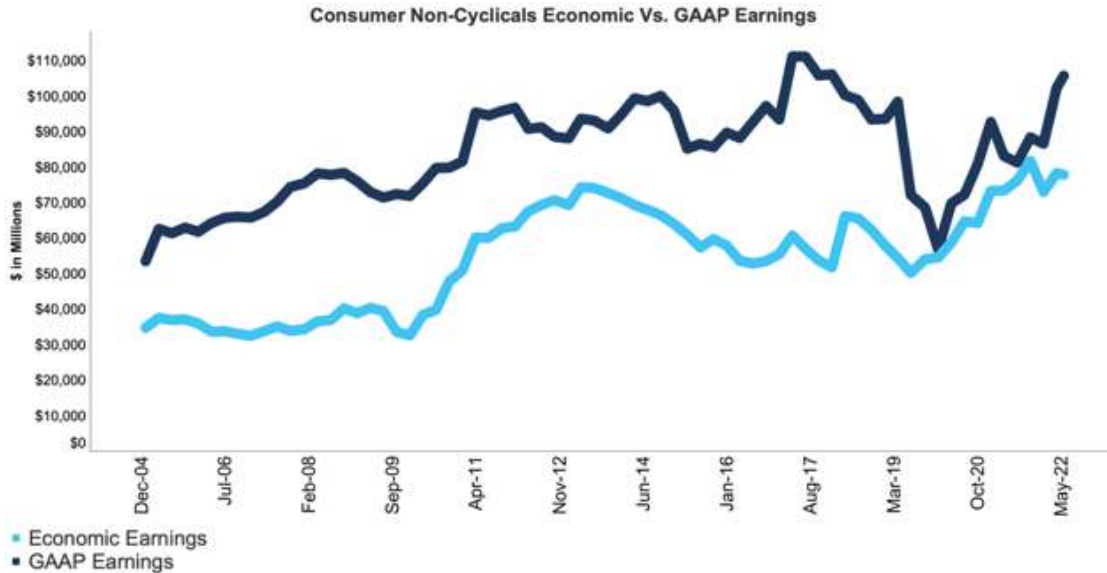
Sources: New Constructs, LLC and company filings. Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period. The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.



### Consumer Non-Cyclicals

Figure 5 shows economic earnings for the Consumer Non-Cyclicals sector, at \$78.0 billion, rose 2% YoY in 1Q22, while GAAP earnings, at \$105.9 billion, rose 30% over the same time.

**Figure 5: Consumer Non-Cyclicals Economic Earnings Vs. GAAP: 2004 – 1Q22**

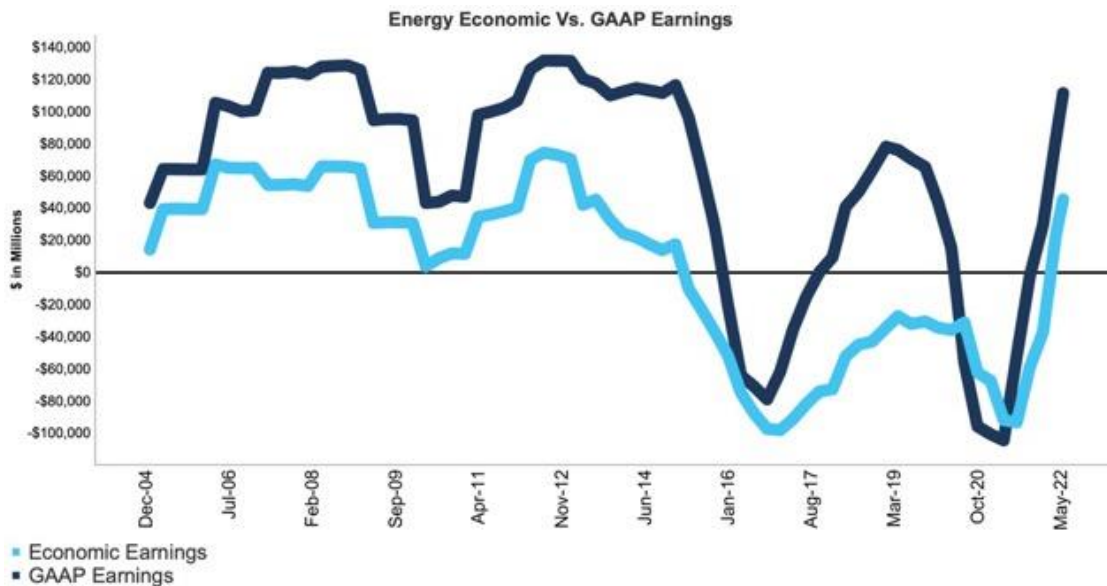


Sources: New Constructs, LLC and company filings. Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period. The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.

### Energy

Figure 6 shows economic earnings for the Energy sector rose from -\$93.1 billion in 1Q21 to \$45.6 billion in 1Q22, while GAAP earnings rose from -\$51.7 billion to \$111.7 billion over the same time.

**Figure 6: Energy Economic Earnings Vs. GAAP: 2004 – 1Q22**



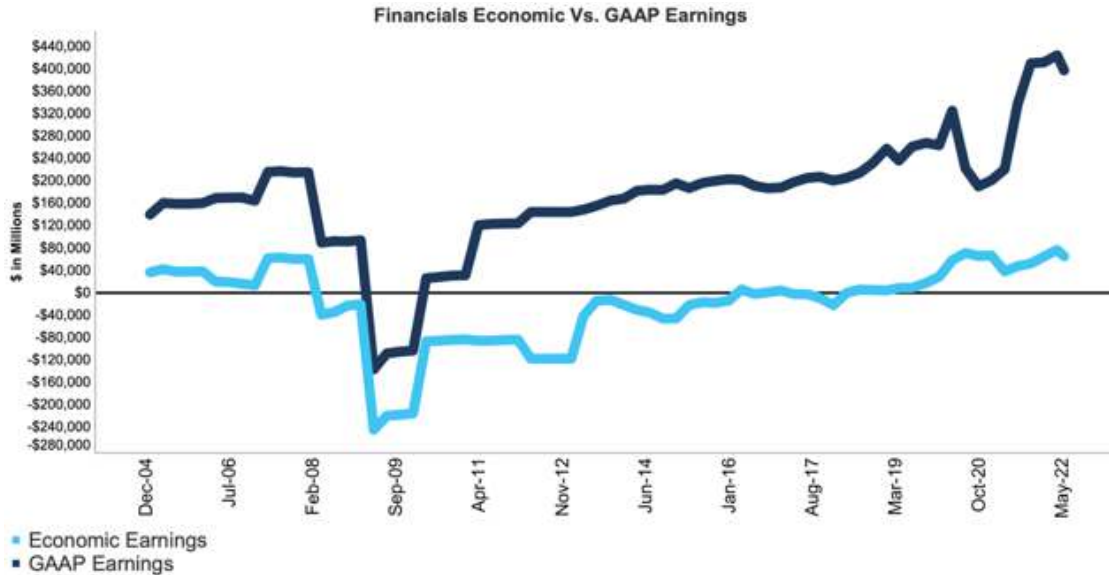
Sources: New Constructs, LLC and company filings. Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period. The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.



### Financials

Figure 7 shows economic earnings for the Financials sector, at \$65.1 billion, rose 37% YoY in 1Q22, while GAAP earnings, at \$397.5 billion rose 18% over the same time.

**Figure 7: Financials Economic Earnings Vs. GAAP: 2004 – 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 S&P 500 constituents were available.

### Healthcare

Figure 8 shows economic earnings for the Healthcare sector, at \$173.9 billion, rose 45% YoY in 1Q22, while GAAP earnings, at \$225.4 billion, rose 54% over the same time.

**Figure 8: Healthcare Economic Earnings Vs. GAAP: 2004 – 1Q22**



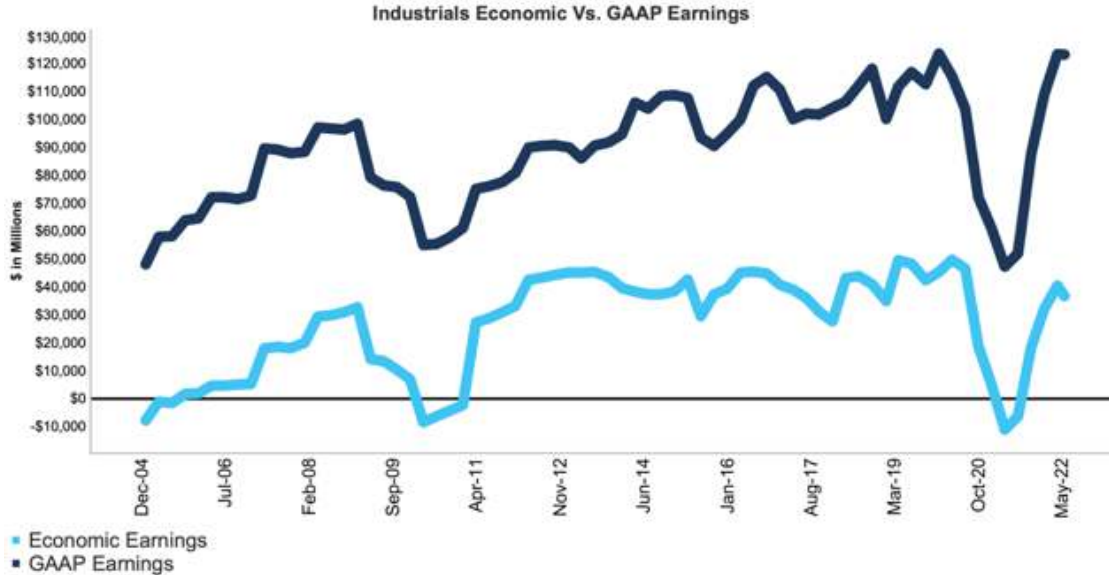
Sources: New Constructs, LLC and company filings. Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period. The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.



### Industrials

Figure 9 shows economic earnings for the Industrials sector rose from -\$6.2 billion in 1Q21 to \$36.8 billion in 1Q22, while GAAP earnings rose from \$52.1 billion to \$123.3 billion over the same time.

**Figure 9: Industrials Economic Earnings Vs. GAAP: 2004 – 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 S&P 500 constituents were available.

### Real Estate

Figure 10 shows economic earnings for the Real Estate sector rose from -\$1.8 billion in 1Q21 to -\$213 million in 1Q22, while funds from operations rose from \$28.2 billion to \$37.9 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: 2004 – 1Q22**



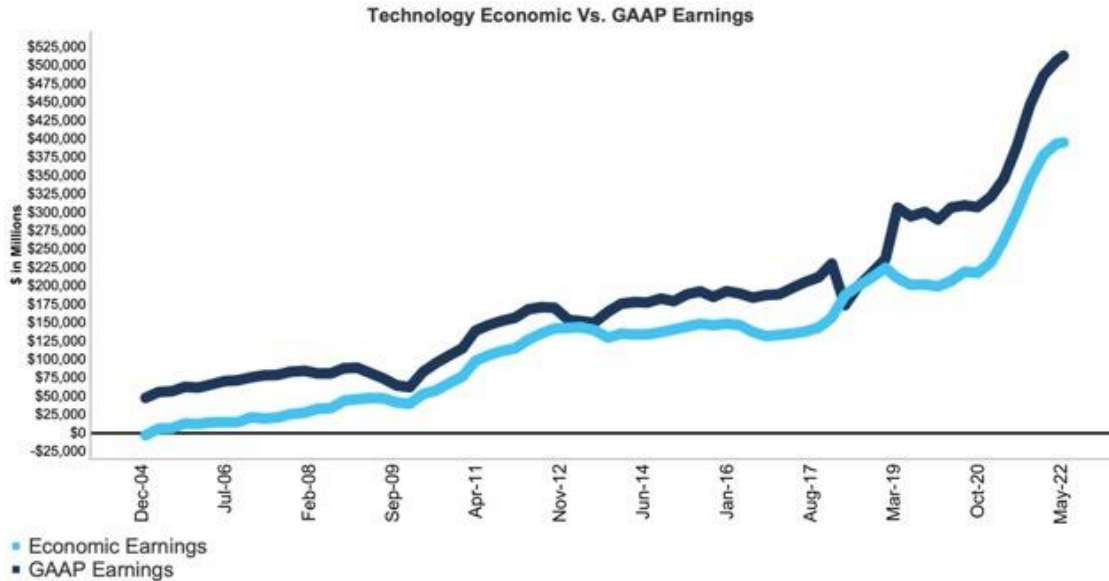
Sources: New Constructs, LLC and company filings. Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period. The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.



### Technology

Figure 11 shows economic earnings for the Technology sector, at \$395.1 billion, rose 31% YoY in 1Q22, while GAAP earnings, at \$513.0 billion, rose 31% over the same time.

**Figure 11: Technology Economic Earnings Vs. GAAP: 2004 – 1Q22**



Sources: New Constructs, LLC and company filings.

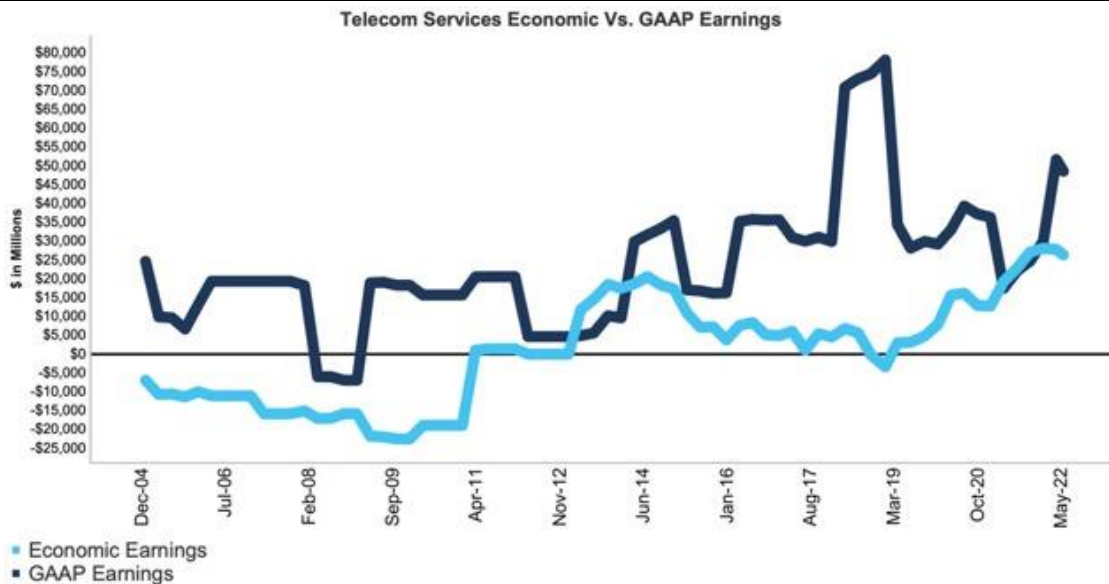
Our economic earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period.

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 S&P 500 constituents were available.

### Telecom Services

Figure 12 shows economic earnings for the Telecom Services sector, at \$26.3 billion, rose 16% YoY in 1Q22, while GAAP earnings, at \$48.5 billion, rose 120% over the same time.

**Figure 12: Telecom Services Economic Earnings Vs. GAAP: 2004 – 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.

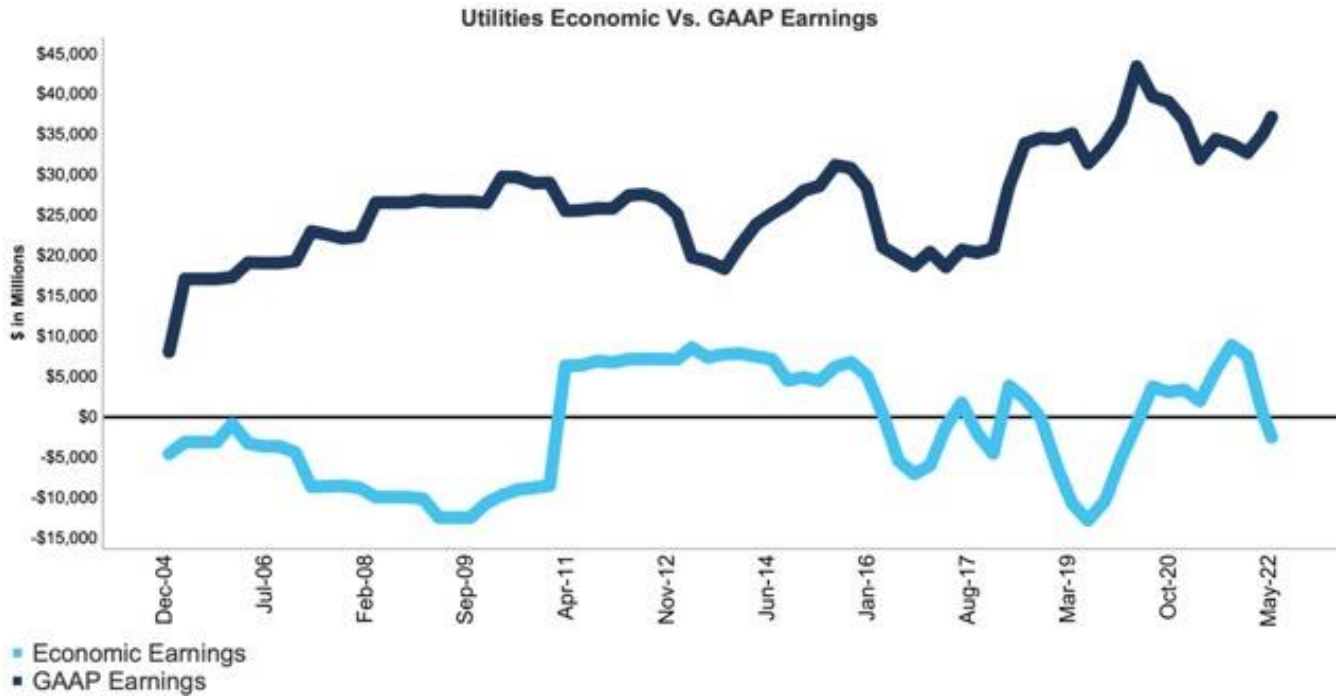
The May 16, 2022 measurement period incorporates the financial data from calendar 1Q22 10-Q, as this is the earliest date for which all the calendar 1Q22 10-Qs for the S&P 500 constituents were available.



### Utilities

Figure 13 shows economic earnings for the Utilities sector fell from \$5.8 billion in 1Q21 to -\$2.5 billion in 1Q22, while GAAP earnings rose from \$34.4 billion to \$37.2 billion over the same time.

**Figure 13: Utilities Economic Earnings Vs. GAAP: 2004 – 1Q22**



Sources: New Constructs, LLC and company filings.

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*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***

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We derive the economic earnings and GAAP Earnings metrics above by summing the Trailing Twelve Month individual S&P 500 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, 1<sup>st</sup> 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 Economic Earnings.” – pp. 16, 2<sup>nd</sup> 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, 5<sup>th</sup> 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, 2<sup>nd</sup> para.

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Key quotes from the paper:

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- “Our results ultimately suggest that Robo-Analysts are a valuable, alternative information intermediary to traditional sell-side analysts.” – pp. 20, 3<sup>rd</sup> para.

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