EARNINGS PREVIEW

1/9/24

4Q23 Earnings: Where Street Estimates Are Too Low & Who Should Beat

While Street Earnings[1] overstate profits for the majority of S&P 500 companies, as shown in Street Earnings Overstated for 75% of S&P 500 in 3Q23, there are many S&P 500 companies whose Street Earnings are lower than their Core Earnings[2].

This report shows:

- the frequency and magnitude of understated Street Earnings in the S&P 500,
- five S&P 500 companies likely to beat 4Q23 earnings, and
- a deep dive into what causes Occidental Petroleum's (OXY) earnings to be understated.

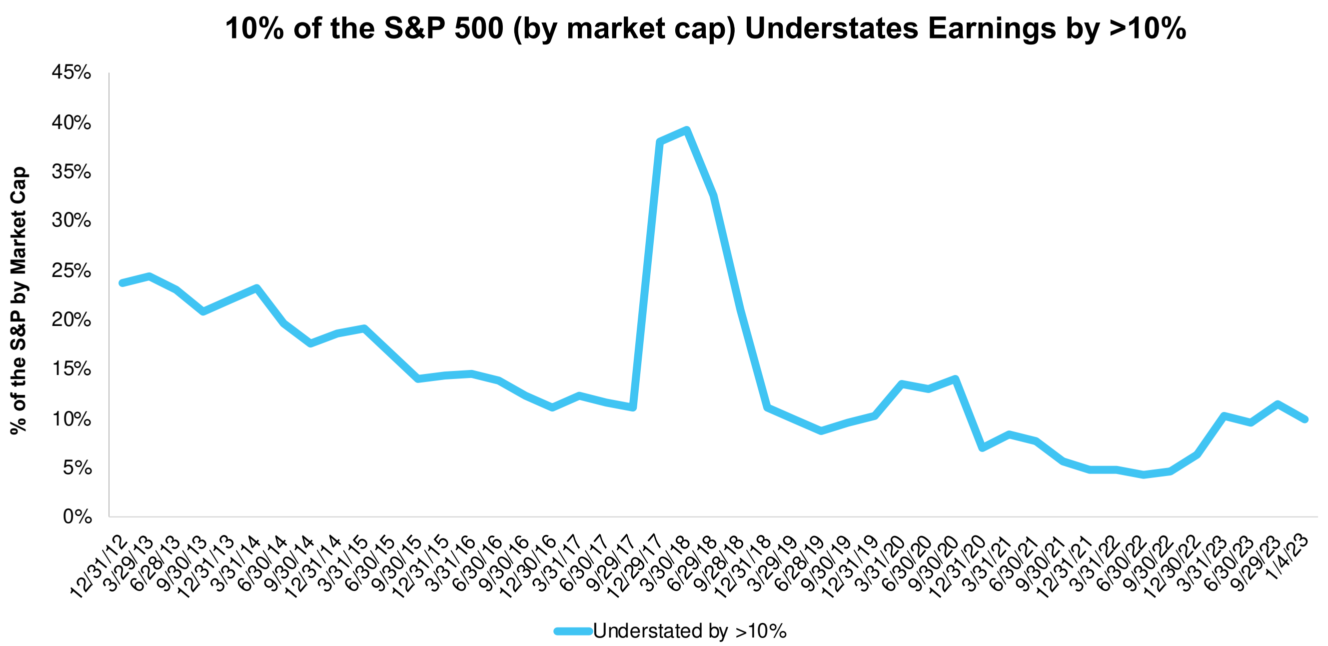
Street EPS Are Lower Than Core EPS for 131 S&P 500 Companies

For 131 companies in the S&P 500, or 26%, Street Earnings are lower than Core Earnings in the trailing-twelve-months (TTM) ended 3Q23. In the TTM ended 2Q23, Street Earnings were understated for 136 companies.

The percentage of the S&P 500 where Street Earnings understate Core Earnings by more than 10% equals 9% (43 companies) in 3Q23, which is down from 47 companies in the TTM ended 2Q23.

Those 43 companies make up 10% of the market cap of the S&P 500 as of 1/4/24, which is down from 11% of the market cap in 2Q23, measured with TTM data in each quarter. See Figure 1.

Figure 1: Understated Street Earnings by >10% as % of Market Cap: 2012 through 1/4/24

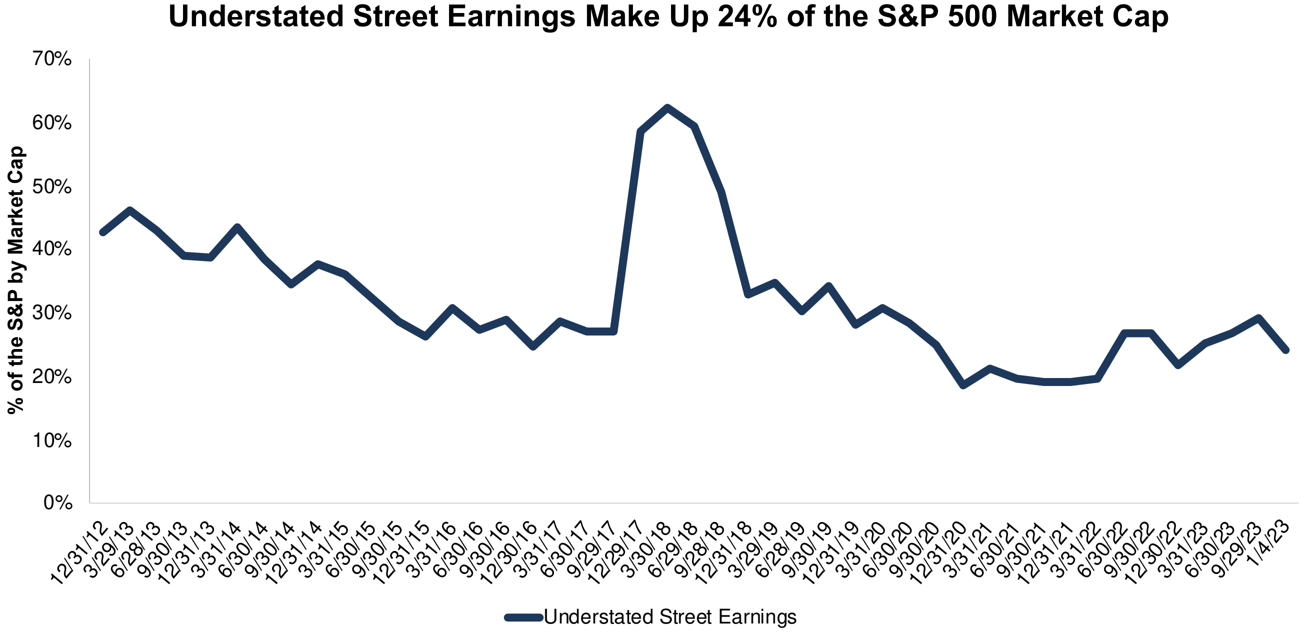


Sources: New Constructs, LLC and company filings.

The 131 companies with understated (by any amount) Street Earnings represent 24% of the market cap of the S&P 500 as of 1/4/24, which is down from 29% in the TTM ended 2Q23. See Figure 2.

[1] Street Earnings refer to Zacks Earnings, which are adjusted to remove non-recurring items using standardized sell-side assumptions.
[2] The Journal of Financial Economics features the superiority of our Core Earnings in Core Earnings: New Data & Evidence.

Figure 2: Understated Street Earnings as % of Market Cap: 2012 through 1/4/24



Sources: New Constructs, LLC and company filings.

Note that this analysis is based on our team analyzing the financial statements and footnotes for ~3,000 10-Ks and 10-Qs filed with the SEC for 3Q23 results. We estimate that the cost of this work for most firms would be around $1 million each quarter. To say the least, there is tremendous value in our rigorous analysis of these filings across so many companies so that our clients can discern the best and worst stocks with unrivaled diligence.

When Street Earnings are lower than Core Earnings, they are understated by an average of 22%, per Figure 3.

Figure 3: Street Earnings Understated by 22% on Average in TTM Through 3Q23

Understated Street Earnings	Understated by >10%	Average Understated %
131 companies	43 companies	22%

Sources: New Constructs, LLC and company filings.

Five S&P 500 Companies Likely to Beat Calendar 4Q23 Earnings

Figure 4 shows five S&P 500 companies likely to beat calendar 4Q23 earnings because their Street EPS estimates are understated. Below we detail the hidden and reported unusual items that caused the understated Street Earnings in the TTM ended 3Q23 for Occidental Petroleum (OXY).

Figure 4: Five S&P 500 Companies Likely to Beat 4Q23 EPS Estimates

Ticker	Name	Street EPS Estimate for 4Q23	Core EPS Estimate for 4Q23*	Street Estimate Understated by
LYV	Live Nation Entertainment	($1.06)	($0.09)	92%
TRGP	Targa Resources	$1.59	$2.44	54%
APA	Apache Corporation	$1.67	$2.11	27%
OXY	Occidental Petroleum	$1.10	$1.30	18%
VRTX	Vertex Pharmaceuticals	$4.08	$4.68	15%

Sources: New Constructs, LLC, company filings, and Zacks
*Assumes Street Distortion as a percentage of Core EPS is the same in 4Q23 as the TTM ended 3Q23

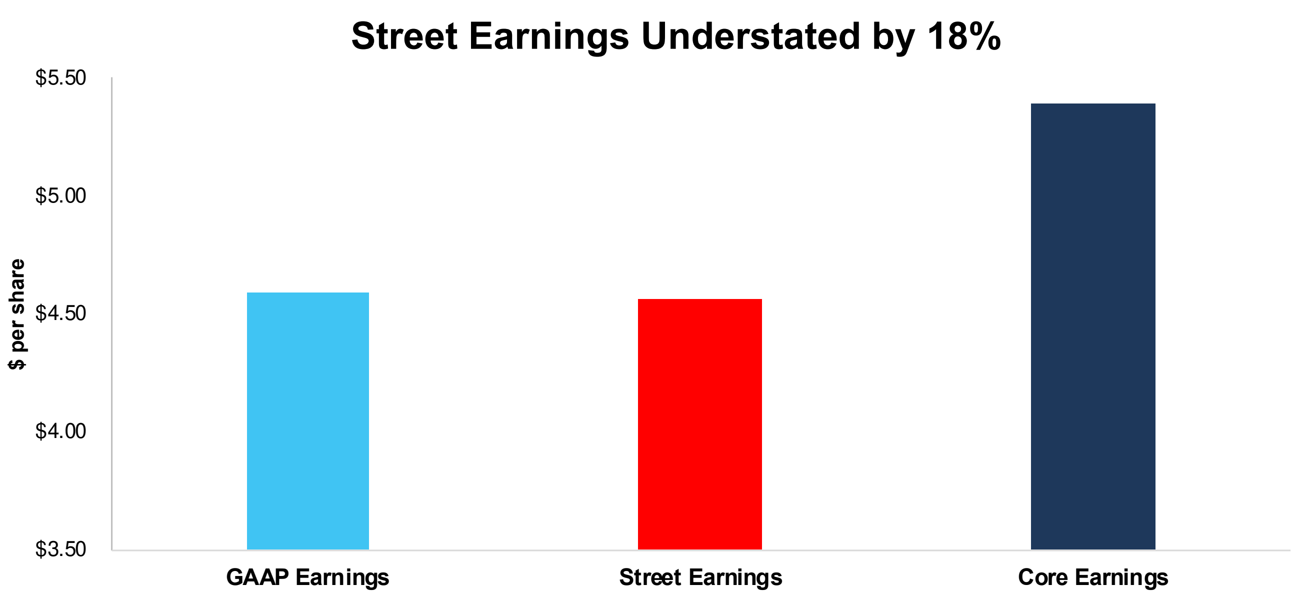
Occidental Petroleum: The Street Underestimates Earnings for 4Q23 by 18%

The Street's 4Q23 EPS estimate of $1.10/share for Occidental Petroleum is $0.20/share lower than our estimate for 4Q23 Core EPS of $1.30/share. Large non-operating expenses and asset impairment charges included in historical EPS drive most of the difference between the Street and Core EPS estimates. After removing these unusual expenses, our analysis of the entire S&P 500 reveals Occidental Petroleum as one of the companies most likely to beat Wall Street analysts' expectations in its 4Q23 earnings report.

Occidental Petroleum's Earnings Distortion Score is Beat. Despite a short-term likelihood to beat earnings expectations, OXY earns a Neutral Stock Rating. Occidental does look undervalued though, with an 8% FCF yield and low price-to-economic book value (PEBV) ratio.

Below, we detail the unusual expenses that materially reduced Occidental's TTM 3Q23 Street and GAAP Earnings. After removing all unusual items, we find that Occidental's TTM Core EPS are $5.39/share, which is higher than the TTM Street EPS of $4.56/share and GAAP EPS of $4.59/share.

Figure 5: Comparing Occidental's GAAP, Street, and Core Earnings: TTM Through 3Q23



Sources: New Constructs, LLC and company filings.

Figure 6 details the differences between Occidental's TTM Core and GAAP Earnings so readers can audit our research. Given the small difference between GAAP and Street Earnings, the adjustments that drive the difference between Core and Street Earnings are likely mostly the same.

Figure 6: Occidental's GAAP Earnings to Core Earnings Reconciliation: TTM 3Q23

	TTM ($ per share)
GAAP Net Income	$4.59
– Hidden Unusual Gains, Net	<$0.01
– Reported Unusual Expenses Pre-Tax, Net	($0.82)
– Tax Distortion	$0.02
– Reported Unusual Expenses After-Tax, Net	($0.02)
= Core Earnings	**$5.39**

Sources: New Constructs, LLC and company filings.

More details:

Total GAAP Earnings Distortion of -$0.81/share, which equals -$784 million, is comprised of the following:

Hidden Unusual Gains, Net = <$0.01/per share, which equals $3.5 million and is comprised of:

- -$21 million in dry hole expense in the TTM period based on an -$84 million expense in the 2022 10-K
- $16 million gain on the sale of limited partner units in the TTM based on a $62 million gain in the 2022 10-K
- $9 million in recognized prior service credit in the 2022 10-K

Reported Unusual Expenses Pre-Tax, Net = -$0.82/per share, which equals -$791 million and is comprised of:

- -$1.0 billion in other operating and non-operating expenses in the TTM period based on
  - -$328 million in 3Q23
  - -$10 million in 2Q23
  - -$308 million in 1Q23
  - -$362 million in 4Q22
- -$232 million reversal of gains on sale of equity investments broken out in 2022 10-Qs and no longer broken out in the 2022 10-K
- -$209 million asset impairment in 2Q23
- -$15 million in losses on interest rates swaps in the TTM period based on $317 million in gains in the 2022 10-K
- -$7 million in Anadarko acquisition related costs in the TTM period based on -$89 million in costs in the 2022 10-K
- $37 million contra adjustment for recurring pension costs. These recurring expenses are reported in non-recurring line items, so we add them back and exclude them from Earnings Distortion.
- $138 million in interest, dividends, and other income in the TTM period based on
  - $50 million in 3Q23
  - $28 million in 2Q23
  - $29 million in 1Q23
  - $31 million in 4Q22
- $505 million in gain on sale of assets in the TTM period based on
  - $192 million in 3Q23
  - $1 million in 2Q23
  - $4 million in 1Q23
  - $308 million in 4Q22

Tax Distortion = $0.02 per share, which equals $23 million

Reported Unusual Expenses After-Tax, Net = -$0.02/per share, which equals -$20 million and is comprised of:

- -$20 million in net income allocated to participating securities in the TTM period based on
  - -$7 million in 3Q23
  - -$4 million in 2Q23
  - -$6 million in 1Q23
  - -$3 million in 4Q22

The $0.83/share of Street Distortion in the TTM ended 3Q23 and $0.81/share in GAAP distortion in the same period highlights that Core Earnings account for a more comprehensive set of unusual items when calculating Occidental's true profitability.

This article was originally published on January 9, 2024.

Disclosure: David Trainer, Kyle Guske II, Hakan Salt, and Italo Mendonça receive no compensation to write about any specific stock, style, or theme.

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It's Official: We Offer the Best Fundamental Data in the World

Many firms claim their research is superior, but none of them can prove it with independent studies from highly respected institutions as we can. Three different papers from both the public and private sectors show:

1. Legacy fundamental datasets suffer from significant inaccuracies, omissions and biases.
2. Only our "novel database" enables investors to overcome these flaws and apply reliable fundamental data in their research.
3. Our proprietary measures of Core Earnings and Earnings Distortion materially improve stock picking and forecasting of profits.

Best Fundamental Data in the World

Forthcoming in The Journal of Financial Economics, a top peer-reviewed journal, Core Earnings: New Data & Evidence proves our Robo-Analyst technology overcomes material shortcomings in legacy firms' data collection processes to provide superior fundamental data, earnings models, and research. More details.

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.

Superior Models

A top accounting firm features the superiority of our ROIC, NOPAT and Invested Capital research to Capital IQ & Bloomberg's in Getting ROIC Right. See the Appendix for direct comparison details.

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.

Superior Stock Ratings

Robo-Analysts' stock ratings outperform those from human analysts as shown in this paper from Indiana's Kelley School of Business. Bloomberg features the paper here.

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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