11/12 2021

MARKET SNAPSHOT

GLENMEDE INVESTMENT MANAGEMENT

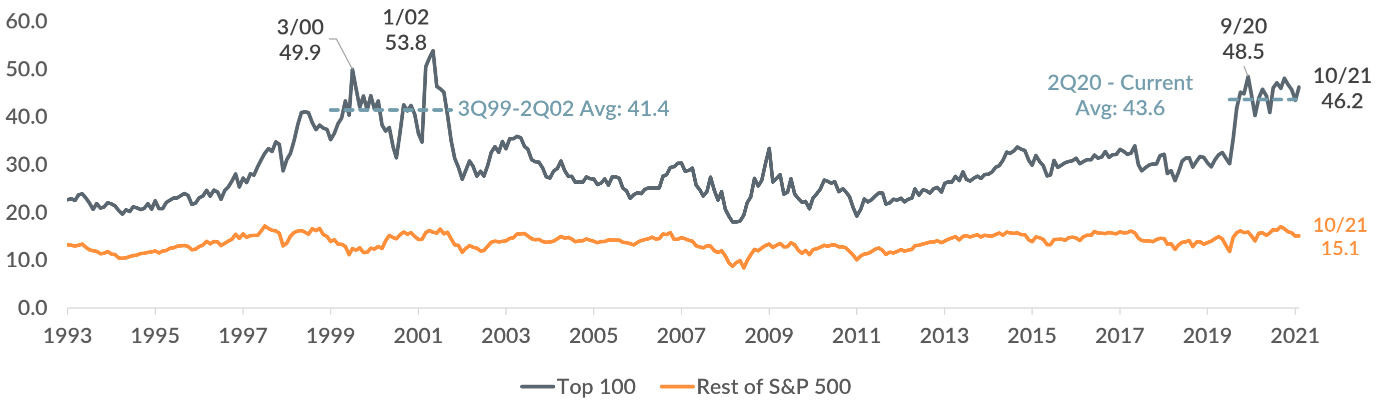
THE RICH GET RICHER - TOP P/E NAMES NEAR HISTORIC LEVELS

The most expensive names based on forward price/earnings (NTM P/E) in the S&P 500 are trading at near-record valuations. As seen in the chart, the forward P/E for the 100 most expensive names in the index is 46.2, which is in the 97th percentile since 1993 and well above the long-term average of 29.7. Meanwhile, the other 400 names in the index have a forward P/E of 15.1, which is only a slight premium to their long-term average of 13.8 and in the 77th percentile since 1993.

Today's environment is comparable to the internet bubble: After trading at elevated levels from late 1999, the top 100 stocks crested at a P/E of 53.8 in January 2002 versus the rest of the names at 15.8. Today, nearly half the companies in the top 100 come from the Information Technology sector. Much like now, in 2002 the top companies had more than double the trailing earnings growth of the rest of the index. In March 2002, the top 100 stocks had 17.7% trailing EPS growth versus the other names at 7.6%. Today, the numbers are 26.8% versus 11.0%, respectively. The advantage was fleeting, however, and by early 2005 the top 100 names and rest of the index were at parity for trailing EPS growth numbers. This implies that the valuation premium the companies enjoyed in 2001 did not translate to superior growth between 2001 and 2005.

Third-quarter 2021 results suggest that the historic growth advantage of the most expensive names may be slipping. Analyst consensus estimates are finally catching up to the strength of the apparent post-COVID earnings rebound, particularly for cyclical names, and are upgrading earnings growth for the whole S&P 500 in 2022 (13.1% versus 9.6% last month) much faster than upgrades to the 100 most expensive names (23.6% versus 22.5% last month). More troubling, though, is that the top P/E companies have begun to post relatively lackluster results this quarter, with an average of a -7.4% EPS surprise versus +9% for the S&P 500 overall, skewed downward by big misses by the likes of Twitter, Caesars Entertainment, Amazon and Match Group. Meanwhile, the 100 most expensive stocks' growth for 2021 has been downgraded from 47.0% at the beginning of earnings season to 42.0%, while the index overall has risen slightly from 46.9% to 47.3%. If these names are priced to perfection, and we see cracks develop in their earnings momentum, this could present an opportunity for active managers with a valuation discipline.

100 Most Expensive Companies by NTM Price/Earnings versus Rest of S&P 500



Sources: FactSet, Compustat Snapshot, Glenmede Investment Management *Data as of 10/31/2021*
Past results are not indicative of future performance