Global Securities Market Bulletin

July 17, 2009
No.11 / 2009

Courtesy: Global Securities Research
Tel: (604) 689-5400   Website: www.globalsec.com
Fax: (604) 647-2160   E-mail: analysts@globalsec.com

COMMENTARY: Investors turn discerning as Q2 earnings season gets underway

Elvis Picardo, CFA

Investors have turned more discerning as the Q2 earnings season gets underway, getting behind stocks that fulfill expectations and punishing those that disappoint on any front. While most of the action so far has occurred in the US, we expect a similar reaction to earnings reports here in Canada as an increasing number of market heavyweights commence reporting from next week onwards. TSX-60 companies that report earnings next week include Canadian National Railway, Suncor, Teck Resources, Husky Energy, Shoppers Drug Mart, Potash, EnCana, and Loblaw.

According to a Bloomberg report, the 38 S&P 500 companies that have reported quarterly results since July 8 have exceeded earnings estimates by an average of 16%. Note that the current expectation for Q2 earnings for the S&P 500 – based on analysts' "bottom-up" EPS estimates as compiled by Standard & Poor's – is for an overall decline of 17.4% from a year earlier.

Here's a synopsis of market reaction to earnings reports from some bellwether stocks so far:

- **General Electric** fell over 6% today, its biggest decline in seven weeks, after it reported a Q2 sales decline that was larger than expectations. Revenue fell 17% to $39.1 billion, well below analysts' average estimate of $41.9 billion. Profit from continuing operations fell 47% from a year ago to $2.87 billion or $0.26 per share, beating the average forecast of $0.24.
- **Bank of America** fell as much as 3% today, despite reporting net income of $3.2 billion, down only 5.5% from a year ago. Analysts' Q2 forecast were all over the map, ranging from a loss of $0.11 per share to EPS of $0.50, due to differences in accounting for unusual items. But after the strong reports posted by JPMorgan Chase and Goldman Sachs earlier this week, investors seemed to be disappointed by further deterioration in BankAm's loan portfolio. Provision for credit losses was unchanged for the second straight quarter at $13.4 billion, while net charge-offs rose 25% from the previous quarter to $8.7 billion and non-performing assets increased 21% to $31.0 billion. BankAm also said that it is not collecting payments on 11.73% of its approximately $170-billion card portfolio, up from 8.62% in the previous quarter.
- **Citigroup** is little changed today after It reported Q2 profit of $4.28 billion, largely due to a gain of $6.7 billion on the sale of its Smith Barney brokerage unit. Excluding that one-time gain, the bank's operating loss of $0.62 per share was wider than the average $0.33 loss estimated by analysts.
- **IBM** gained over 3% today, bringing its gains for this week to 14%, after it reported Q2 earnings late yesterday. The company reported net income rose 12% from a year ago to $3.1 billion or $2.32 per share – largely due to aggressive cost cuts – beating the average forecast of $2.02. A 13% drop in sales, which fell to $23.3 billion, resulted in IBM missing analysts' average estimate of $23.5 billion. However, the company boosted its guidance for 2009 EPS to at least $9.70, up $0.50 from a previous forecast of at least $9.20.
- **Google** fell as much as 3.6% today after it reported Q2 sales growth slowed to 2.9% from 6.2% in Q1. Net income rose 19% to $1.48 billion, while EPS (excluding expenses such as stock-based compensation) of $5.36 exceeded analysts' average forecast of $5.08.
- In Canada, **Nexen** yesterday fell 6.6% after it reported declines in profit and revenues that were bigger than expected. Net income plunged 95% from a year ago to $20 million or $0.04 per share, a huge miss form analysts' forecast of $0.24, while net sales fell 42% to $1.2 billion, also missing the $1.3 billion forecast.
- **Nokia** plunged 14% yesterday for its biggest one-day decline in five years after it cut its

forecasts for market share and profitability. The world's biggest maker of mobile phones said its market share would be little changed this year, compared with a previous forecast of an increase. Nokia said that operating margin in its main division would also be little changed in the second half of 2009 from the first half; it had earlier forecast operating margin in the "teens." Although net income of EUR 380 million or EUR 0.10 was higher than analysts' forecast of EUR 361 million, sales of EUR 9.9 billion missed the EUR 10.1 billion forecast.

As the above examples demonstrate, companies cannot afford to disappoint investors on any front. Performance expectations have been ratcheted higher in recent months, and it should come as no surprise if many companies find it difficult to beat them in an economic environment that continues to be quite challenging. Against this backdrop, we believe it may be prudent to wait until a company reports Q2 earnings before taking a position in the stock.

Market Snapshot at 12:15 am

S&P TSX	10376.24	+71.82	**Commodities**			**Yields (%)**	**Can.**	**US**
TSX Venture	1091.48	-6.32	Canadian $	89.49	-0.02	90 Day T-Bill	0.13	0.17
DJIA	8728.37	+16.55	Gold (Spot)	937.65	+0.31	2-Year Bond	1.20	0.99
S&P 500	938.66	-2.08	Oil (WTI-Aug.)	63.60	+1.58	10-Yr.Bond	3.48	3.64
NASDAQ	1883.55	-1.48	CRB Index	245.05	+4.10	30-Yr. Bond	4.01	4.52

Thought for the Day

"The time to repair the roof is when the sun is shining."– John F. Kennedy