

The Great Earnings Mirage?

- **US equities are not merely expensive. They are increasingly reliant on an extraordinary acceleration in profits. The coming earnings season will test whether the “E” can keep doing the heavy lifting.**
- **Markets seem to be treating extraordinary earnings growth as the new normal. What if it isn’t?**



By **OLIVER MÜLLER**,
CHIEF INVESTMENT OFFICER,
ACCRESCO INVESTMENT MANAGEMENT

There is a comforting trick in equity valuation: if the price looks expensive, let the earnings catch up.

That, increasingly, is the argument supporting US equities. Yes, the S&P 500 trades at a rich valuation. But profits are growing rapidly. Yes, the index has risen substantially. But earnings are catching up. And yes, multiples look elevated against history, but perhaps the “E” in the P/E ratio will simply grow into the price.

There is nothing inherently wrong with that argument. Ultimately, earnings underpin shareholder value, and strong earnings growth can justify a surprisingly high share price.

The more interesting question is how much we are now asking earnings to do.

As the third-quarter reporting season begins, consensus expectations have become extraordinary. S&P 500 earnings are expected to rise by roughly 32% this year. Analysts have been raising rather than cutting their forecasts. The expected earnings trajectory has moved sharply above its longer-term trend. And much of the apparent comfort in today’s valuation multiples depends on those forecasts being delivered.

Perhaps they will be. But investors should at least recognise just how much optimism is now embedded in the denominator.

AN EXTRAORDINARY ACCELERATION

Let’s start with the obvious: 2026 is shaping up to be an exceptional year for corporate profits.

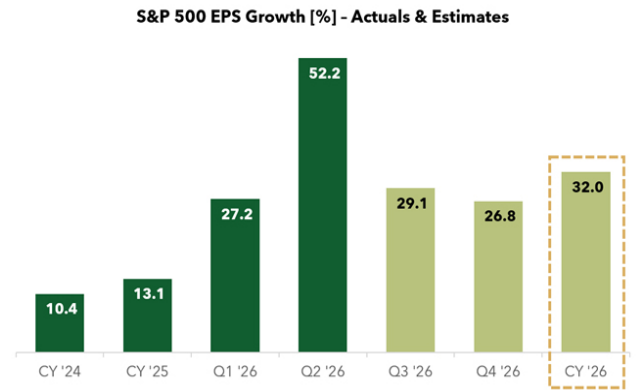
S&P 500 earnings per share are expected to rise by roughly 32%, compared with growth of around 13% in 2025 and 10% in 2024. In other words, earnings growth this year is expected to be roughly three times the rate achieved just two years ago.

The second quarter was particularly striking. Headline EPS growth exceeded 50%. Some of that reflected sizeable non-operating gains at a handful of companies, so it would be misleading to treat the full number as a clean measure of underlying corporate momentum. Even after allowing for those distortions, however, earnings growth remained exceptionally strong.

Normally, one might expect some moderation after a quarter like that. Consensus does not.

Current estimates imply roughly 29% earnings growth in the third quarter and 27% in the fourth. This is not a forecast for one spectacular quarter followed by a return to normality. It assumes earnings growth remains exceptionally elevated through year-end.

That may prove correct. But it is an unusually high bar.



A BREAK ABOVE TREND

The numbers become even more interesting when placed in a longer-term context.

S&P 500 earnings rose from about \$119 per share in 2016

to \$275 in 2025. That works out at compound annual growth of approximately 9.7%, a respectable rate achieved through a decade that included a pandemic, a recession, an inflation shock and a dramatic shift in interest rates.

Consensus now assumes a sharp break above that trajectory.

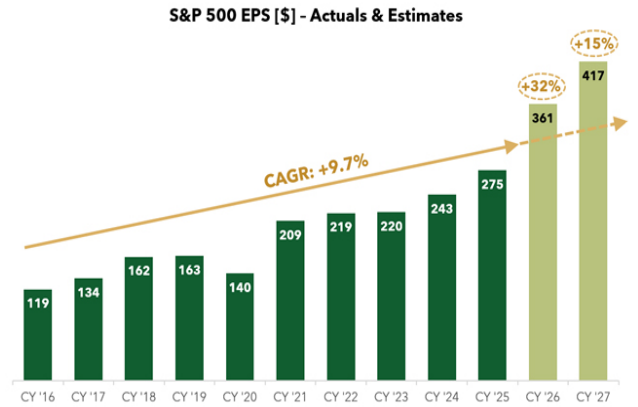
EPS is expected to rise to roughly \$361 in 2026 and \$417 in 2027. That means growth of 32% this year, followed by another 15% next year. Taken together, earnings would rise by approximately 52% in just two years. At the previous 9.7% trend rate, an increase of that magnitude would ordinarily have taken considerably longer.

None of this means the forecasts are wrong. Economies, industries and companies do not grow in straight lines. Productivity can improve. Margins can expand. Technology can create genuine step-changes in profitability. Artificial intelligence may yet prove to be one of them.

But the distinction matters.

Investors are no longer being asked merely to believe in another year of decent earnings growth. They are being asked to accept the possibility that the earnings trajectory itself has shifted upward.

Are we seeing the beginning of a new earnings regime, or several years of growth being pulled forward?



THE BAR IS STILL RISING

There is another unusual feature of the current reporting season: analysts have not been lowering the hurdle.

The familiar pre-earnings-season pattern is for estimates to drift down. Companies guide conservatively, analysts trim forecasts, and the market enters reporting season with a little breathing room. That is one reason the ritual of “beating expectations” has become such a regular feature of quarterly results.

Across the last 20 quarters, analysts lowered S&P 500 EPS estimates during the first two months of the quarter in 13 cases. They raised them in only six and left them unchanged once.

Recently, that pattern has reversed.

Estimates have risen in four of the past five quarters. Ahead of the second quarter of 2026 they increased by 2.6%; ahead of the current third-quarter season they have risen another 1.3%.

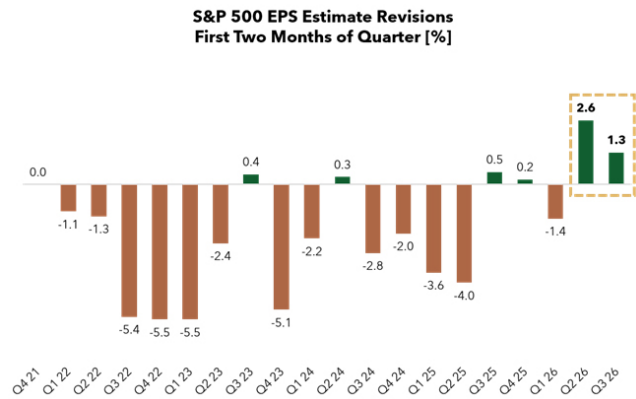
That leaves less room for an easy beat.

Companies are entering this reporting season with exceptionally high earnings-growth expectations and consensus estimates that have already been revised higher. The usual pre-season cushion has largely disappeared.

The hurdle is not merely high. It is still being raised.

Investors are being asked to accept the possibility that the earnings trajectory itself has shifted upward.

Earnings expectations are accelerating. They have moved well above their longer-term trend.



ARE EPS ESTIMATES JUSTIFIED?

Corporate earnings and economic growth are not the same thing.

The S&P 500 is global. Its sector composition differs markedly from that of the US economy. Large listed companies can gain market share, improve margins and grow internationally even when domestic economic growth is merely respectable.

But over the cycle, earnings and nominal GDP have tended to move in the same direction. Earnings are simply much more volatile. Operating leverage and changing margins mean that profits tend to accelerate much faster during expansions and fall much harder during downturns.

That makes the current divergence worth watching.

Consensus expects S&P 500 earnings growth to accelerate dramatically even as nominal US GDP growth shows nothing remotely comparable. Historically, sustained earnings acceleration has usually coincided with improving nominal economic momentum.

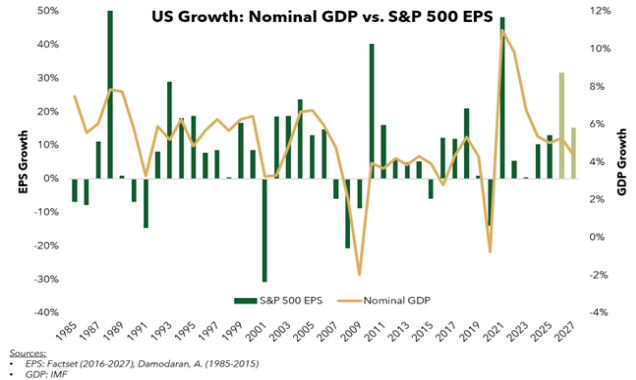
If GDP is not doing the work, something else must.

Margins can expand. Companies can buy back shares. Productivity can improve. Artificial intelligence may reduce costs or increase output. And the index itself may continue to tilt towards highly profitable businesses whose economics bear less resemblance to the broader economy than they once did.

All are plausible.

But collectively they amount to an important assumption: there needs to be a bridge between the economic growth we can observe and the profit growth investors are expecting.

The existence of such a bridge is entirely possible. Its durability is the more important question.



THE “E” IS DOING THE HEAVY LIFTING

This matters because valuations leave little room for disappointment.

The S&P 500 currently trades at roughly 20.4 times forward earnings. That is above its five-year average, its ten-year average and its twenty-year median.

Yet 20 times earnings can still be made to look relatively comfortable if the earnings denominator is growing at 30%.

Rapid expected profit growth does some useful work. As earnings rise, the denominator expands, allowing a high index level to coexist with a forward multiple that remains somewhere around 20 times.

But suppose earnings do not follow the extraordinary path currently embedded in consensus. Suppose instead that they simply continue to compound at their longer-term rate of approximately 9.7%.

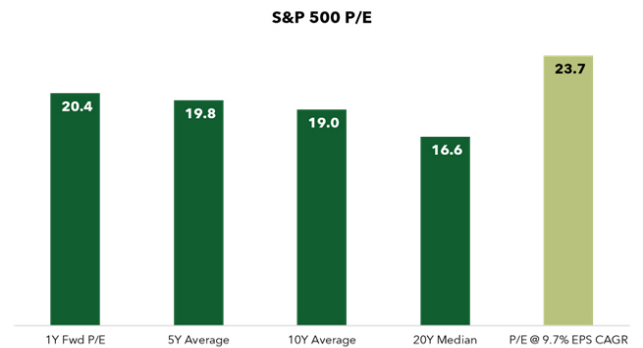
On that basis, the implied P/E rises to roughly 23.7 times earnings, just shy of the historic peak of approximately 24.4 times.

That is the uncomfortable arithmetic beneath the current valuation debate.

The market does not merely need earnings to grow. It needs

them to grow considerably faster than their historical trend for today’s valuation to look relatively ordinary.

The “E” is doing a remarkable amount of heavy lifting.



VALUATION WITHOUT FORECASTS

There is another way to look at the problem: take forecasts out of the equation altogether.

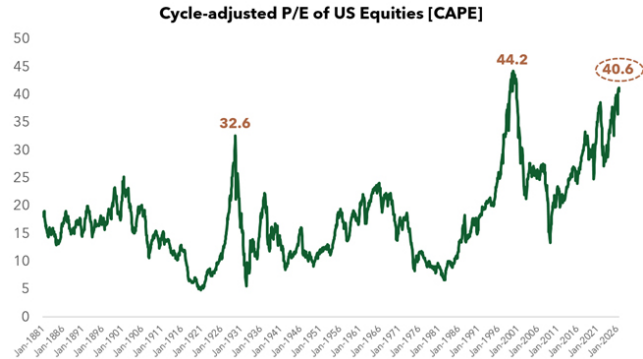
The cyclically adjusted price-to-earnings ratio, or CAPE, compares today’s market price with the average of the previous ten years of inflation-adjusted earnings. Unlike the conventional forward P/E, it does not rely on analyst estimates of what companies might earn next year or the year after.

On that measure, US equities currently trade at approximately 40.6 times earnings. That is well above the 32.6 times reached in 1929 and only modestly below the 44.2 times recorded around the peak of the dot-com bubble.

CAPE has its limitations. The composition of the US equity market has changed enormously over the past century, accounting standards have evolved, and today’s largest businesses often require far less physical capital than those of earlier generations. Comparing 2026 directly with 1929 should therefore never be treated as a perfect like-for-like exercise.

But that is not really the point.

The point is that the apparent comfort provided by the forward P/E relies heavily on exceptional future earnings growth being delivered. Take those assumptions away and valuation looks stretched. Or, more simply: CAPE shows how expensive the market looks without that.



The argument here is not that the earnings boom must be a mirage.

Corporate America has repeatedly demonstrated an ability to increase margins, innovate, become more productive and confound those who underestimate its adaptability. The largest companies in the S&P 500 are extraordinarily profitable businesses. It is entirely possible that AI, automation and the continuing rise of capital-light business models support a structurally higher level of profitability.

But there is an important difference between believing earnings can grow and building valuations that increasingly require exceptional growth.

That is where investors find themselves today.

Earnings expectations are accelerating. They have moved well above their longer-term trend. Analysts are raising forecasts as reporting season approaches. The macro economy is not accelerating at anything like the same pace. And valuations become considerably harder to justify if earnings merely return to something resembling normal.

That makes this third-quarter reporting season more important than the usual collection of beats, misses and guidance revisions.

It will provide another test of the assumption increasingly underpinning US equity valuations: that extraordinary earnings growth is not merely a cyclical surge, but the beginning of something more durable.

If that assumption is right, today’s valuations may eventually look less extraordinary. If it is wrong, the mirage may become easier to see.