



All Cap Index & Sectors: Earnings Distortions Flash Warning Signs for Equity Investors (Free, Abridged)

GAAP earnings remain overstated despite a year-over-year (YoY) rise in [Core Earnings](#) for all eleven sectors of the NC 2000¹ through the trailing-twelve-months (TTM), ended 1Q22, just as they did in [2021](#).

This report is an abridged and free version of [All Cap Index & Sectors: Earnings Distortions Flash Warning Signs For Equity Investors](#), one of our quarterly reports on [fundamental market and sector trends](#).

The full version of the report analyzes [Core Earnings](#)²³ and GAAP earnings of the NC 2000⁴ and each of its sectors. Last quarter's analysis is [here](#). The full report is available to clients with a [Pro or higher](#) membership or can be purchased [here](#).

Buy the Full Version of This Report

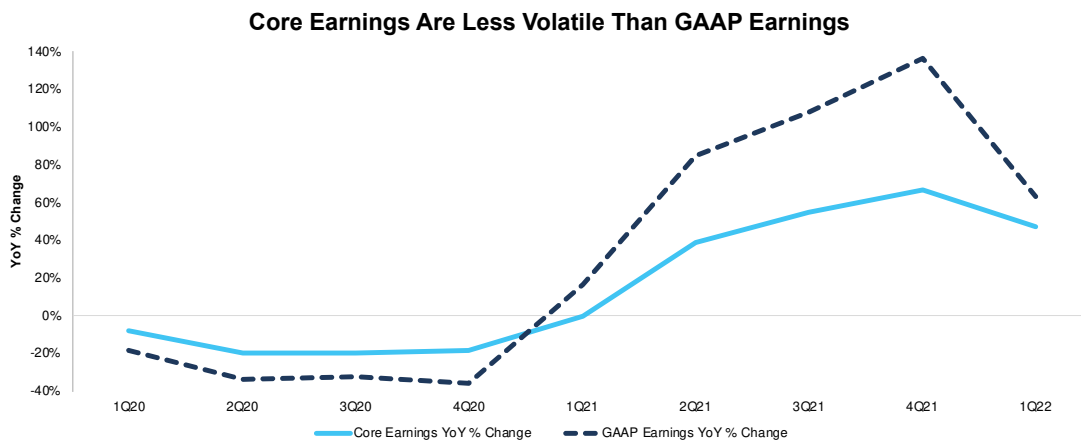
Core Earnings Are More Reliable than GAAP Earnings

Figure 1 in the [full report](#) shows GAAP Earnings for the NC 2000 overstate Core Earnings by far more than before the Financial Crisis. The last time GAAP Earnings exceeded Core Earnings was in the TTM ended June 2007. Not long after, GAAP earnings took a dive.

GAAP Earnings rose much faster over the last year, at 63%, compared to 47% for Core Earnings. Since 2020, corporate profits have been much less volatile than indicated by GAAP earnings. For instance:

- In 2020, GAAP earnings fell 36% YoY compared to an 18% fall for Core Earnings.
- In 2021, GAAP earnings rose 136% YoY compared to a 67% rise for Core Earnings.
- In the TTM ended 1Q22, GAAP earnings rose 63% YoY compared to a 47% rise for Core Earnings.

Figure 1: NC 2000 Core Earnings Vs. GAAP Earnings YoY Percent Change: 1Q20 – 1Q22



Sources: New Constructs, LLC and company filings.

Our Core 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 1Q22 10-Qs, as this is the earliest date for which all the calendar 1Q22 10-Qs for the NC 2000 constituents were available.

¹ The NC 2000 consists of the largest 2000 U.S. companies by market cap in our coverage. Constituents are updated on a quarterly basis (March 31, June 30, September 30, and December 31). We exclude companies that report under IFRS and non-U.S. ADR companies.

² Core Earnings enable investors to overcome the flaws in legacy fundamental data and research, as proven in [Core Earnings: New Data & Evidence](#), written by professors at Harvard Business School (HBS) & MIT Sloan for [The Journal of Financial Economics](#).

³ Based on the latest audited financial data, which is the 10-K for calendar 2021 in most cases.

⁴ The NC 2000 consists of the largest 2000 U.S. companies by market cap in our coverage. Constituents are updated on a quarterly basis (March 31, June 30, September 30, and December 31). We exclude companies that report under IFRS and non-U.S. ADR companies.



This report leverages our cutting-edge [Robo-Analyst technology](#) to deliver [proven-superior](#)⁵ fundamental research and support more cost-effective fulfillment of the [fiduciary duty of care](#).

GAAP Earnings Widely Overstated at the Individual Company Level⁶

42%, or 830 of the companies in the NC 2000, report GAAP Earnings that overstate Core Earnings for the TTM ended 1Q22. When GAAP Earnings overstate Core Earnings, they do so by an average of 38%, per Figure 2. The overstatement was greater than ten percent for 20% of companies. For comparison, in the TTM ended 2021 the percent of companies that overstate Core Earnings was 40%.

The 830 companies with overstated GAAP earnings make up 52% of the market cap of the NC 2000.

Figure 2: NC 2000 GAAP Earnings Overstated by 38% On Average

Overstated GAAP Earnings	Overstated by >10%	Average Overstatement %
830 companies	397 companies	38%

Sources: New Constructs, LLC and company filings.
We use Funds from Operations (FFO) for Real Estate companies rather than GAAP Earnings.

Key Details on Select NC 2000 Sectors

The Energy sector saw the largest YoY improvement, \$139.2 billion in Core Earnings, which rose from -\$3.4 billion in 1Q21 to \$135.8 billion in 1Q22.

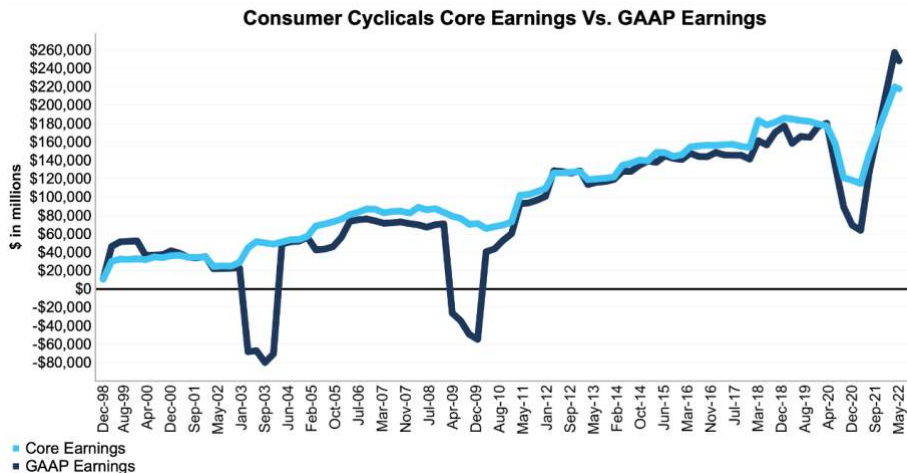
The Technology sector generates the most Core Earnings, at \$486.9 billion, and grew Core Earnings by 30% YoY in 1Q22. On the flip side, the Real Estate sector has the lowest Core Earnings at \$36.3 billion, and the Consumer Non-cyclicals sector, at just 9%, had the weakest YoY growth in 1Q22.

Below we highlight the Consumer Cyclical sector and a stock with some of the most Earnings Distortion (i.e. overstated GAAP earnings) in the sector.

Sample Sector Analysis⁷: Consumer Cyclical

Figure 3 shows Core Earnings for the Consumer Cyclical sector, at \$217.9 billion, rose 49% YoY in 1Q22, while GAAP earnings, at \$248.3 billion, rose 96% over the same time.

Figure 3: Consumer Cyclical Core Earnings Vs. GAAP: 1998 – 1Q22



Sources: New Constructs, LLC and company filings.
Our Core Earnings analysis is based on aggregated TTM data for the sector constituents in each measurement period. The May 16, 2022 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 NC 2000 constituents were available.

⁵ Our research utilizes our [Core Earnings](#), a more reliable measure of profits, 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](#).

⁶ Overstated companies include all companies with Earnings Distortion >0.1% of GAAP earnings.

⁷ The full version of this report provides analysis for all eleven sectors.



GAAP Earnings Overstatement Details: WideOpenWest Inc. (WOW)

Below, we detail the [hidden and reported](#) unusual items that GAAP Earnings miss but that we capture in Core Earnings for WideOpenWest Inc. (WOW). After adjusting for unusual items, we find that WideOpenWest’s Core Earnings of -\$87.8 million, or -\$1.06/share are much worse than reported GAAP Earnings of \$766.6 million, or \$9.25/share.

Below, we detail the differences between Core Earnings and GAAP Earnings so readers can audit our research.

Figure 4: WideOpenWest’s GAAP Earnings to Core Earnings Reconciliation

	TTM 1Q22 (\$ per share)
GAAP Net Income	\$9.25
– Hidden Unusual Gains, Net	\$0.07
– Reported Unusual Gains Pre-Tax, Net	\$0.17
– Tax Distortion	(\$0.06)
– Reported Unusual Gains After-Tax, Net	\$10.12
= Core Earnings	(\$1.06)

Sources: New Constructs, LLC and company filings.

More details:

Total Earnings Distortion of \$10.30/share, which equals \$854.4 million, is comprised of the following:

Hidden Unusual Gains, Net = \$0.07/per share, which equals \$6 million and is comprised of

- \$6 million in non-recurring professional fees, M&A integration, and restructuring expense in the TTM period based on
 - Reversal of \$14 million in 4Q21 as non-recurring fees were disclosed in prior Qs but no longer disclosed in 2021 10-K
 - [-\\$8 million](#) in 2Q21

Reported Unusual Gains Pre-Tax, Net = \$0.17/per share, which equals \$14 million and is comprised of

- \$18 million in other income in the TTM period based on
 - [\\$9 million](#) in 1Q22
 - [\\$7 million](#) in 4Q21
 - [\\$2 million](#) in 3Q21
- [-\\$0.4 million](#) loss on sale of assets in 1Q22
- -\$3 million loss in the TTM period based on [-\\$3 million](#) loss on early extinguishment of debt in 2021 10-K

[Tax Distortion](#) = -\$0.06/per share, which equals -\$4.9 million

Reported Unusual Gains After-Tax, Net = \$10.12/per share, which equals \$839 million and is comprised of

- \$839 million in income from discontinued operations in the TTM period based on
 - [\\$265 million](#) in 4Q21
 - [\\$539 million](#) in 3Q21
 - [\\$35 million](#) in 2Q21

This article originally published on [June 2, 2022](#).

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

We derive the Core Earnings and GAAP Earnings metrics above by summing the trailing-twelve-month individual NC 2000 constituent values for Core 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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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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