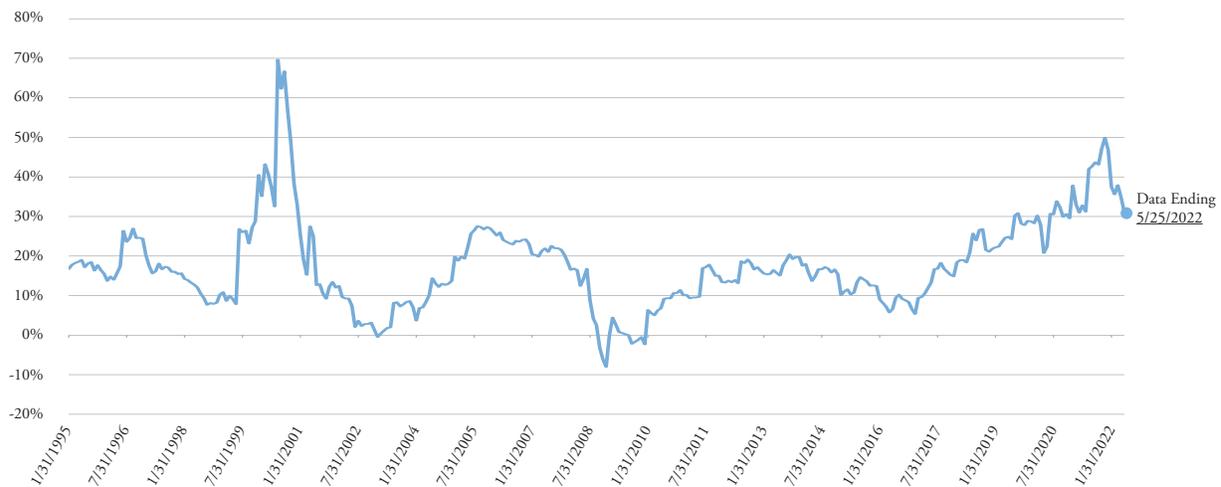


## Valuations Improve, But Are Growth Estimates Too High?

The stock market has experienced P/E compression thus far in 2022, with the P/E of the S&P 500 (based on next-twelve-month earnings) dropping from 22.7x at the beginning of the year to 17.4x as of 5/25. The P/E of the Russell 1000 Growth Index has declined even more during the same period, dropping from 33.3x to 22.8x. The good news is that some of the unusually high valuation of the Russell 1000 Growth Index relative to the S&P 500 has been corrected, although the relative valuation is still at the higher end of its historical range.

### Russell 1000 Growth P/E Relative to S&P 500 (Based on Next-12-Months Estimated Earnings)



Data from 1/31/1995–5/25/2022  
Source: Bloomberg

On the other hand, long-term earnings growth expectations are still relatively high. The chart below illustrates the average of estimates of long-term earnings growth among Russell 1000 Growth Index companies. Today's average figure of around 20% is much higher than usual. While it is certainly possible that future earnings growth will be well above historical levels, it is more likely that expectations for future growth may be revised downward. Worth noting, the median figure for earnings growth is close to its historical average, indicating that the average figure is impacted by higher

### Estimated Long Term EPS Growth Estimates, Russell 1000 Growth Constituents



Monthly data from 3/31/2002–4/30/2022  
Source: FactSet

estimates among a handful of “high-flying” growth stocks, which may account for their generally higher valuations. However, high growth expectations have not prevented many of these “high-flying” stocks, such as Netflix, Roku, Peloton, etc., from significantly underperforming this year.

So far this year, our bias toward high quality, reasonably valued growth companies has been well rewarded in terms of relative performance versus growth indices. While the overall market environment will likely remain volatile in the near term, we believe that there are many good long-term investment opportunities in growth stocks for disciplined investors.

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## REFERENCED INDICES

*(Indices are unmanaged and are not available for direct investment.)*

**Russell 1000 Growth Index**—The Russell 1000<sup>®</sup> Growth Index is a market capitalization weighted index that measures the performance of those Russell 1000<sup>®</sup> companies with higher price-to-book ratios and higher forecasted growth values.

**S&P 500 Index**—The S&P 500 Stock Index is a market capitalization weighted index and consists of 500 stocks chosen for market size, liquidity and industry group representation.

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