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TRIVARIATE RESEARCH

STOCKS THAT GET CHEAPER MISS ESTIMATES MORE

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RESEARCH SUMMARY & CONCLUSIONS

Background: Last year, we published a research note concluding that relying on valuation is generally not helpful for picking stocks. In today's note, we delve deeper into why this is the case. We looked at the top 900 stocks by market cap. and divided them into deciles based on price-to-forward earnings, excluding companies that are not profitable.

There's a relationship between trailing growth and valuation: Only stocks in the cheapest decile that just saw a quarterly decline in their price-to-forward earnings have less than 50% of the companies growing their year-over-year EPS growth. **Unsurprisingly, a higher percentage of more expensive stocks grow their earnings year-over-year than cheap stocks.** Moreover, for every decile of price-to-forward earnings, a higher percentage of companies grow earnings year-over-year that just had their multiple expand than companies that just saw their multiple contract.

Buying a cheap stock that just got cheaper is a bad idea: We assessed the percentage of stocks that have positive 3-month forward earnings revisions by how much their price-to-forward earnings changes over the three months PRIOR to their earnings reports. There are two important observations:

- 1) **Companies that are cheap are MUCH less likely to subsequently beat consensus EPS estimates than companies that are expensive.**
- 2) **Companies that get more expensive – no matter what their starting valuation level – are far more likely to subsequently get upward revisions than companies that just saw lower multiples over the last quarter.** Using mean-reverting valuation in time frames like 3-6-months to pick stocks is a money-losing idea. Buying stocks that are cheap and just got cheaper is a good way to lose money – instead these should be SHORT ideas.

INVESTMENT CONCLUSIONS

For example, 74% of stocks in the 2nd most expensive decile on price-to-forward earnings (9th cheapest) with price-to-forward earnings multiple expansion over the previous quarter have upward earnings revisions the next quarter. On the contrary, only 49% of stocks in the cheapest decile that got cheaper the previous quarter end up with upward revisions. Buying cheap stocks that got cheaper is a way to decrease your chance of buying a stock with upward revisions.

Changes in valuation also lead to changes in gross margin forecasts: Stocks that just got more expensive have a higher chance of having upward revisions to their gross margin outlook than stocks that just got cheaper – independent of whether they were cheap or expensive to start out with. The change in valuation is associated with the change in the gross margin outlook. In fact, stocks in the three most expensive deciles on price-to-forward earnings that got more expensive over the last quarter are the only three deciles where more than 50% of the stocks had upward gross margin revisions. On the contrary, only 41% of stocks that are in the cheapest quintile and saw multiple contraction over the last quarter get subsequent upward gross margin revisions.

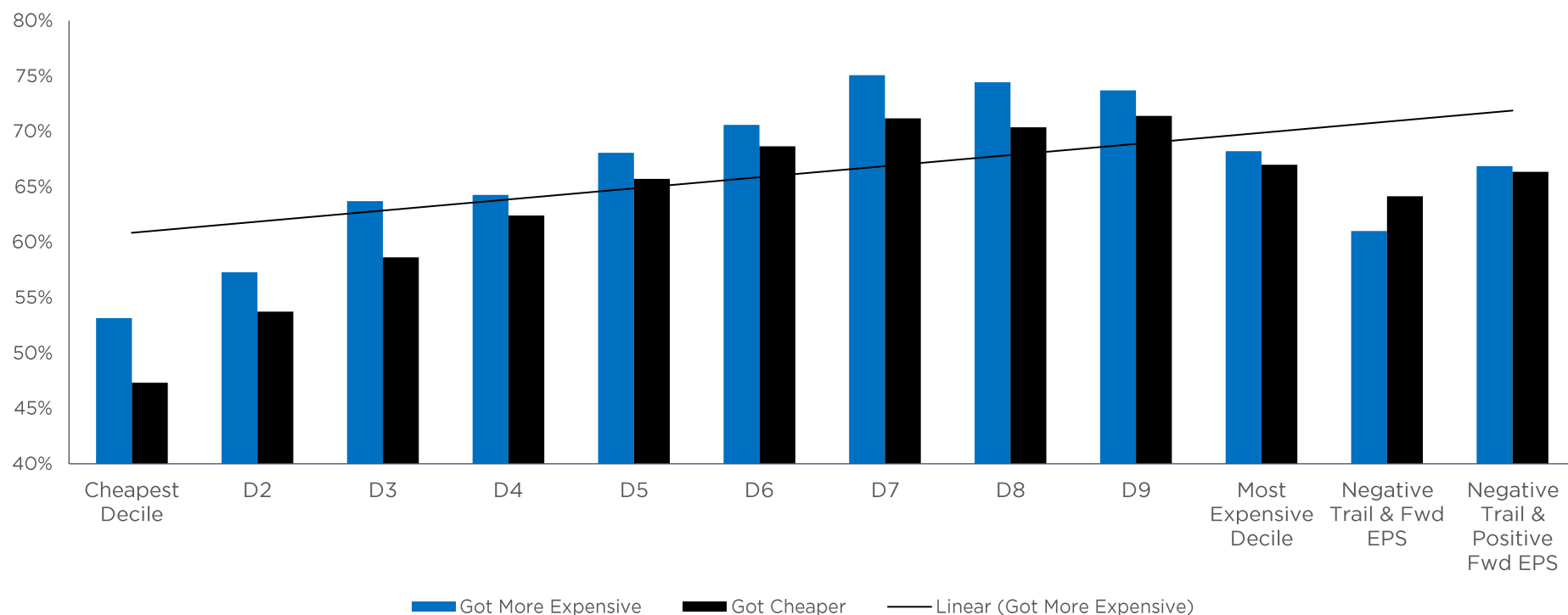
There is a serial correlation to stocks that just beat estimates: On average about 70% of companies beat EPS estimates. The percentage of stocks that beat estimates if they beat last quarter is 76%, but the percentage that beat estimates if they have beaten six quarters in a row is 86%. Some companies consistently and continuously surprise analysts to the upside on the earnings line. On the flip side, the likelihood a company beats EPS estimates conditional on just missing goes down each consecutive quarter of missing. 57% beat one quarter after they missed, but only 38% of companies beat estimates if they missed the last four quarters in a row.

On Slide 8 we shows stocks and their “implied” revisions based on recent changes to their price-to-forward earnings multiples that report earnings next week.

THERE'S A RELATIONSHIP BETWEEN EPS GROWTH AND VALUATION

We looked at the top 900 stocks by market cap. and broke it into deciles based on price-to-forward earnings, stripping out companies that don't make money. Only stocks in the cheapest decile that just saw a quarterly decline in their price-to-forward earnings have less than 50% of the companies growing their year-over-year EPS growth. Unsurprisingly, a higher percentage of more expensive stocks grow their earnings than cheap stocks. Moreover, for every decile of price-to-forward earnings, a higher percentage of companies that just had their multiple expand grow earnings year-over-year than companies that just saw their multiple contract.

Percentage of Stocks with Higher YoY Quarterly EPS
By Prior 3-Month Expansion or Contraction of Price-to-Fwd Earnings Multiple
Top 900 US Equities
Through End-December, 2025

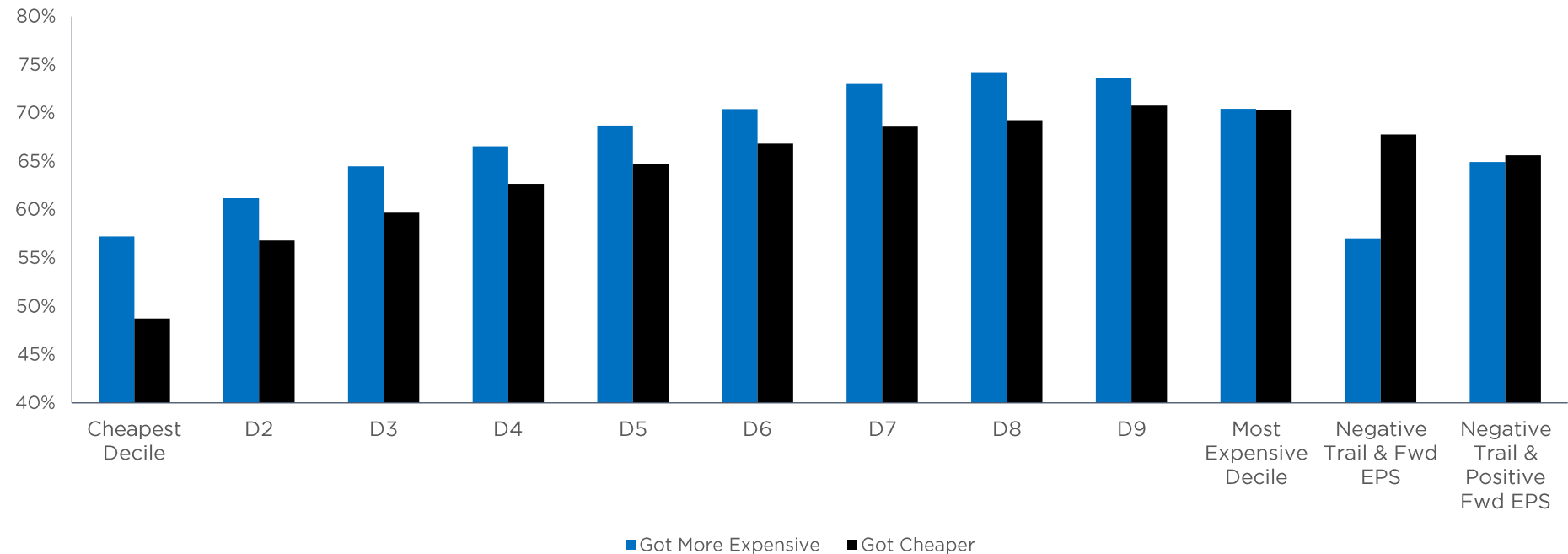


Source: Trivariate Research

BUYING A CHEAP STOCK THAT GOT CHEAPER ON PEF IS A BAD IDEA

Below we show the percentage of stocks that have positive 3-month forward earnings revisions by how much their price-to-forward earnings changes over the three months PRIOR to their earnings reports. There are two important observations: 1) Companies that are cheap are MUCH less likely to subsequently beat consensus EPS estimates than companies that are expensive. 2) Companies that get more expensive – no matter what their starting valuation level – are far more likely to have subsequent upward revisions. For example, 74% of stocks in the 2nd most expensive decile on price-to-forward earnings (9th cheapest) with price-to-forward earnings multiple expansion over the previous quarter have upward earnings revisions. 57.2% of stocks that are in the cheapest decile of price-to-forward earnings subsequently have upward revisions. Only 49% of stocks in the cheapest decile that got cheaper the previous quarter end up with upward revisions. Buying cheap stocks that got cheaper is a way to decrease your chance of buying a stock with upward revisions. For companies that lose money, the signal is less reliable.

Percentage of Stocks with Positive 3-Month EPS Revisions
By Prior 3-Month Expansion or Contraction of Price-to-Fwd Earnings Multiple
Top 900 US Equities
Through End-December, 2025

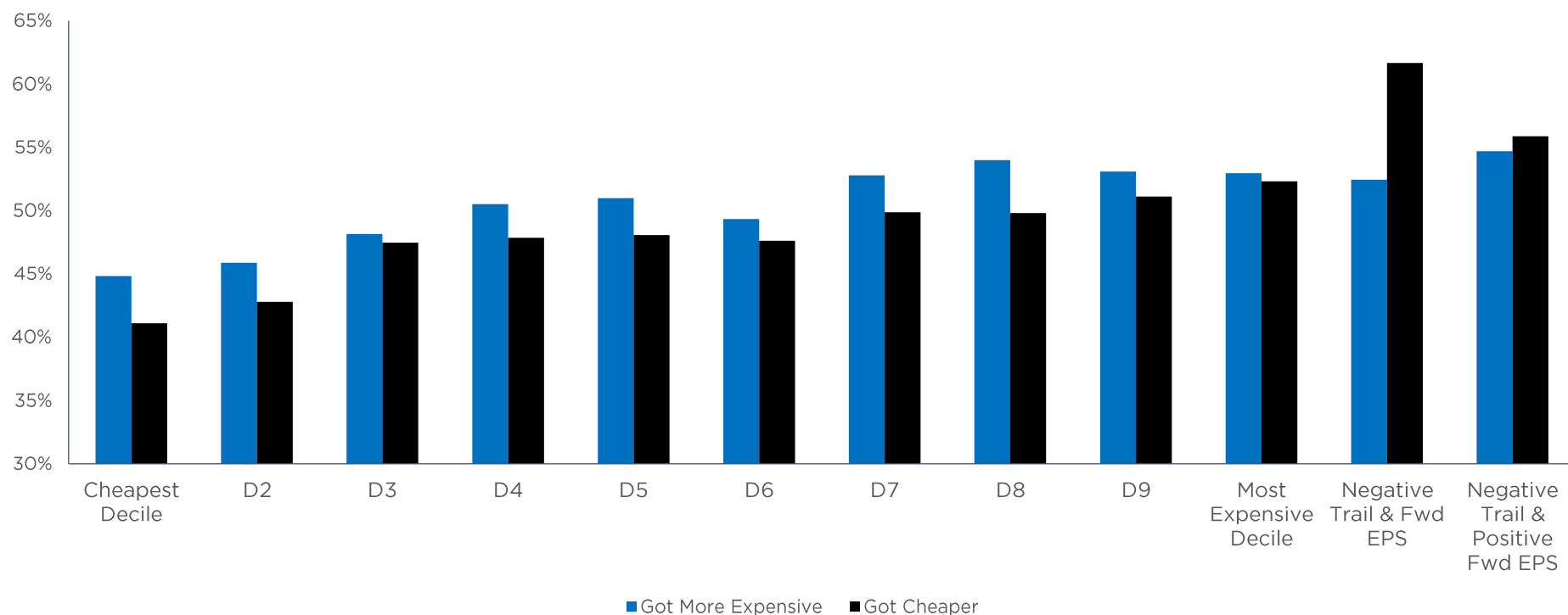


Source: Trivariate Research

VALUATION CHANGE AND LEVEL PREDICT GROSS MARGIN REVISIONS

Stocks that just got more expensive have a higher chance of having upward revisions to their gross margin outlook than stocks that just got cheaper – independent of whether they were cheap or expensive to start out with. The change in valuation is associated with the change in the gross margin outlook. In fact, the stocks in the three most expensive deciles on price-to-forward earnings that got more expensive over the last quarter are the only three deciles where more than 50% of the stocks had upward gross margin revisions. On the contrary, only 41% of stocks that are in the cheapest quintile on price-to-forward earnings and saw multiple contraction over the last quarter get subsequent upward gross margin revisions.

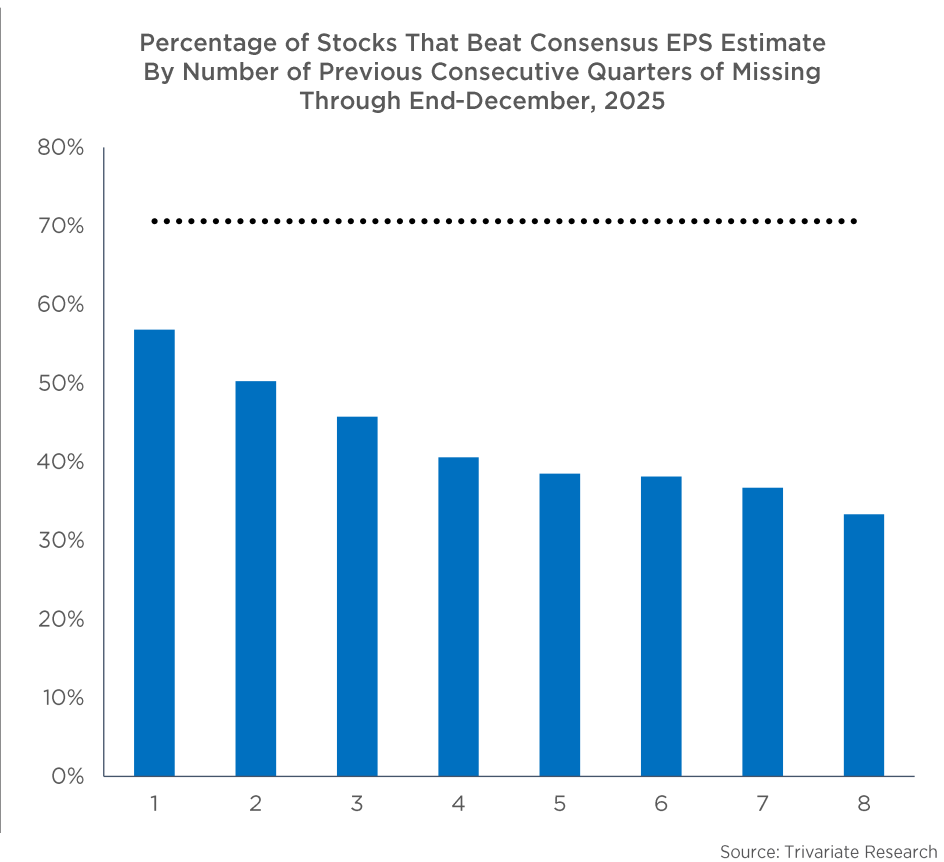
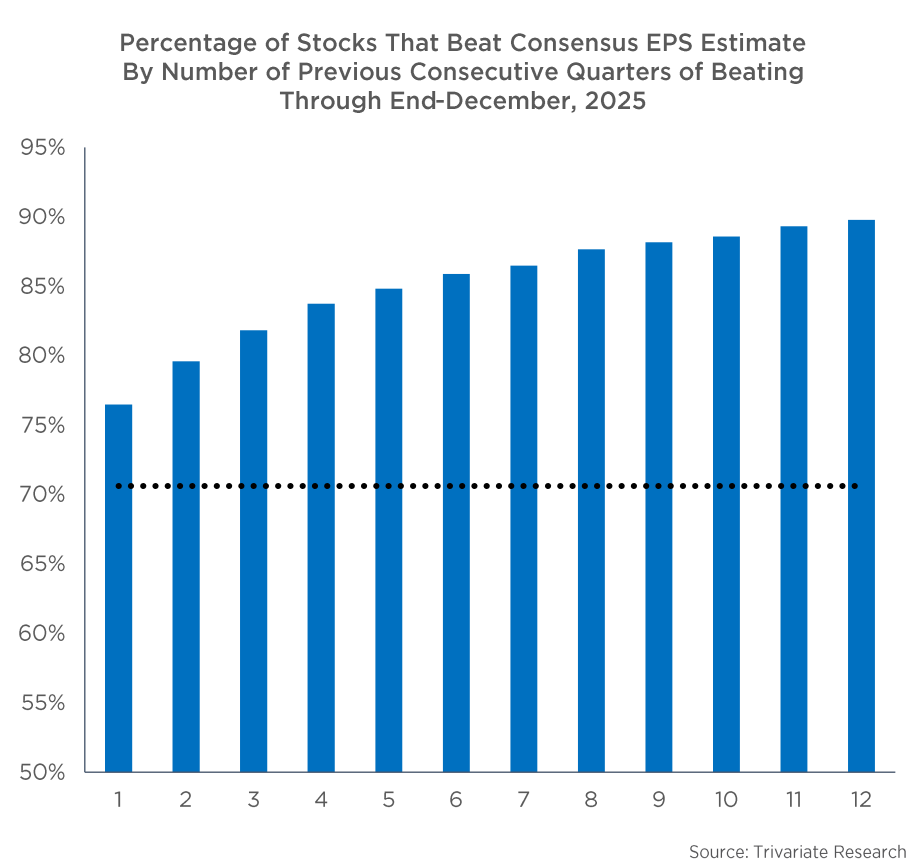
Percentage of Stocks with Positive 3-Month Gross Margin Revisions
By Prior 3-Month Expansion or Contraction of Price-to-Fwd Earnings Multiple
Top 900 US Equities
Through End-December, 2025



Source: Trivariate Research

THERE IS A SERIAL CORRELATION TO BEATING AND MISSING EPS

Moreover, and importantly, there is a serial correlation to stocks that just beat estimates. The percentage of stocks that beat estimates if they beat last quarter is 76%, but the percentage that beat estimates if they have beaten six quarters in a row is 86%. Some companies either fundamentally create upside or have enough flexibility to continuously surprise analysts to the upside (left). On the flip side, the chance a company beats EPS estimates conditional on just missing goes down each consecutive quarter of missing. On average about 70% of companies beat EPS estimates. 57% beat one quarter after they missed, but only 38% of companies beat estimates if they missed the last four quarters in a row (right).



UPCOMING EARNINGS RELEASES AND “IMPLIED” REVISIONS

Below we show stocks that report earnings next week that have gotten more expensive recently and have beat consensus EPS estimates for the last 3 quarters, therefore increasing their chance of upward earnings revisions (left). On the right, we show stocks that have gotten cheaper and therefore have a higher probability of downward revisions.

Upcoming Earnings Releases
Top Quintile of 3-Month Change in Price-to-Forward Earnings
& Have Beat Consensus EPS for Last 3 Quarters
As of January 21st, 2025

Report Date	Ticker	Company	Market Cap. (US \$Bn.)
1/27/2026	RTX	RTX Corporation	264.80
1/29/2026	CRS	Carpenter Technology Corporation	16.77
1/29/2026	DOV	Dover Corporation	28.60
1/29/2026	LHX	L3Harris Technologies, Inc.	65.06
1/29/2026	PH	Parker-Hannifin Corporation	119.28
1/30/2026	XOM	Exxon Mobil Corporation	563.46
2/2/2026	IDXX	IDEXX Laboratories, Inc.	55.61
2/2/2026	TER	Teradyne, Inc.	36.32
2/3/2026	AME	AMETEK, Inc.	50.74
2/3/2026	LITE	Lumentum Holdings Inc.	25.70
2/3/2026	ATI	ATI Inc.	16.94
2/3/2026	EMR	Emerson Electric Co.	84.10
2/4/2026	LLY	Eli Lilly and Company	965.69
2/4/2026	COHR	Coherent Corp.	34.39
2/4/2026	EVR	Evercore Inc.	14.40
2/5/2026	CAH	Cardinal Health, Inc.	49.53
2/5/2026	BE	Bloom Energy Corporation	35.61
2/5/2026	EL	The Estée Lauder Companies Inc.	42.48
2/5/2026	XPO	XPO, Inc.	17.59
2/5/2026	RBC	RBC Bearings Incorporated	15.89

Source: Trivariate Research

Upcoming Earnings Releases
Bottom Quintile of 3-Month Change in Price-to-Forward Earnings
As of January 21st, 2025

Report Date	Ticker	Company	Market Cap. (US \$Bn.)
1/26/2026	BRO	Brown & Brown, Inc.	26.65
1/26/2026	WRB	W. R. Berkley Corporation	25.67
1/27/2026	ROP	Roper Technologies, Inc.	43.56
1/27/2026	KMB	Kimberly-Clark Corporation	33.20
1/27/2026	UNH	UnitedHealth Group Incorporated	315.01
1/28/2026	ADP	Automatic Data Processing, Inc.	103.94
1/28/2026	NOW	ServiceNow, Inc.	129.99
1/28/2026	META	Meta Platforms, Inc.	1544.98
1/28/2026	FICO	Fair Isaac Corporation	36.49
1/28/2026	URI	United Rentals, Inc.	59.82
1/28/2026	T	AT&T Inc.	166.60
1/28/2026	MSFT	Microsoft Corporation	3300.79
1/29/2026	V	Visa Inc.	622.01
1/29/2026	RMD	ResMed Inc.	37.77
1/29/2026	TT	Trane Technologies plc	87.66
1/29/2026	AJG	Arthur J. Gallagher & Co.	64.22
1/29/2026	MA	Mastercard Incorporated	473.76
1/29/2026	SYK	Stryker Corporation	138.80
1/30/2026	SOFI	SoFi Technologies, Inc.	32.40
2/2/2026	PLTR	Palantir Technologies Inc.	394.05

Source: Trivariate Research

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