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Markets and Economies

Equities: Three Quick Points on Earnings, Valuations, and the Bull Market

Are earnings still healthy? Are p/e ratios stretched? Here, we address these and other questions about the current market advance.

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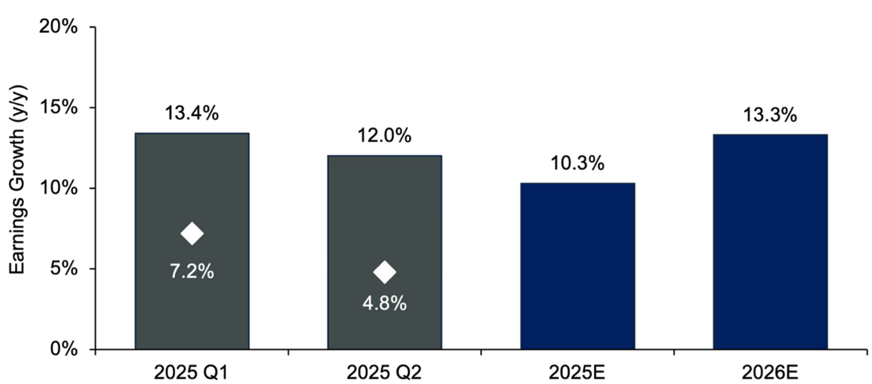
Equity markets faced challenges in the early part of the year, as global trade and tariff uncertainty created headwinds that were stronger than the expected tailwinds from more supportive U.S. fiscal and monetary policy. But investors have shaken off concerns over tariffs and the economy to bid stocks higher. Here, we focus on three key factors supporting equities in the current market.

1. Earnings Remain Strong

The equity markets have shown some resilience as first- and second-quarter earnings for the S&P 500® Index beat expectations by a wide margin. (See Figure 1.) Earnings growth for the rest of the year, and for 2026, is expected to be in double digits.

Figure 1. After Upside Surprises, Earnings Strength Is Expected to Continue

Reported and forecast earnings for the S&P 500 Index for the indicated periods



Source: FactSet. Data as of 8/31/2025. Diamonds represent earnings estimates at the beginning of each bar's respective quarter.

Past performance is not a reliable indicator or guarantee of future results. The historical data shown in the chart above are for illustrative purposes only and do not represent any specific portfolio managed by Lord Abbett.

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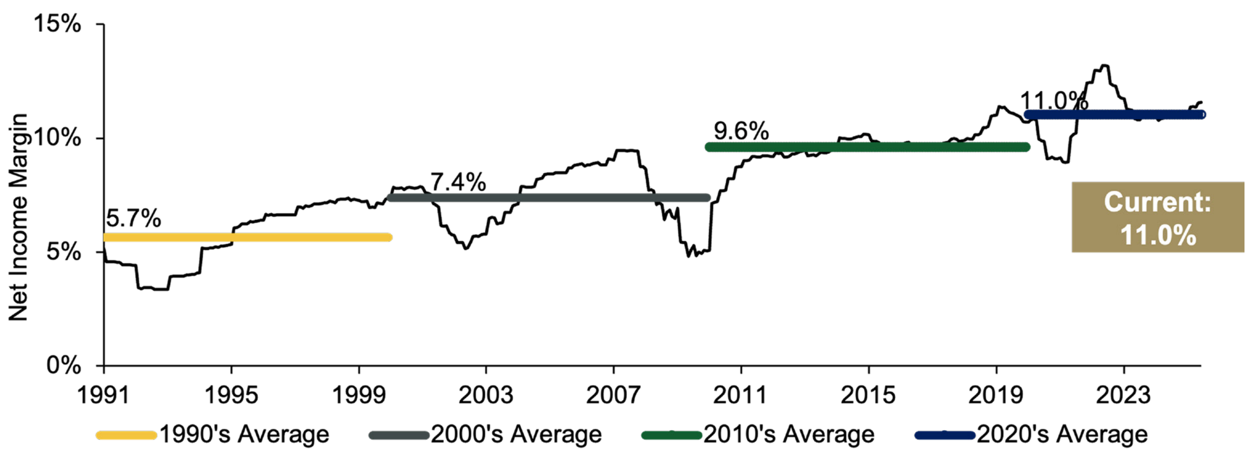
Amid the challenges posed by tariff uncertainty and the prospect of slowing U.S. economic growth, the robust earnings picture provides an encouraging sign of resilience.

2. Valuations Need to Be Seen in Context

Based on forward price-to-earnings (P/E) ratios, stocks are more expensive than they have been on average over the last 40 years. The average forward P/E for the S&P 500 over the last 40 years is 16.7x. The market is currently trading at roughly 23x. But we think a few points merit consideration here. We believe the companies dominating the market now are better equipped to generate consistent earnings growth and deliver value to shareholders. Forty years ago, the net income margin of the S&P 500 was below 6%; now, companies on average are earning over 11% (see Figure 2). Free-cash-flow margins were below 5% in the mid-1980s; now, they are over 11%. The amount of money that companies returned to shareholders in the form of dividends and buybacks was 25% as a percentage of return on equity; now, it's 70%.

Figure 2. S&P 500 Profitability Is at an All-Time High

Net income margin for the S&P 500 Index (monthly), January 1, 1991–August 31, 2025



Source: FactSet. Data as of 8/31/2025. Net income margin is a financial ratio used to calculate the percentage of profit a company produces from its total revenue, measuring the amount of net profit a company obtains per dollar of revenue gained.

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Why is this the case? Company structures have changed drastically over the past 40 years. Back then, the companies leading the market were economically cyclical—think manufacturing and utilities. Now, innovation—think technology and communications—makes up a much larger percentage of the market capitalization of the S&P 500. These companies have leaner balance sheets and more efficient business models, which make them more profitable. This is all to say that we think the market is more expensive because companies are better at generating profits and creating value.

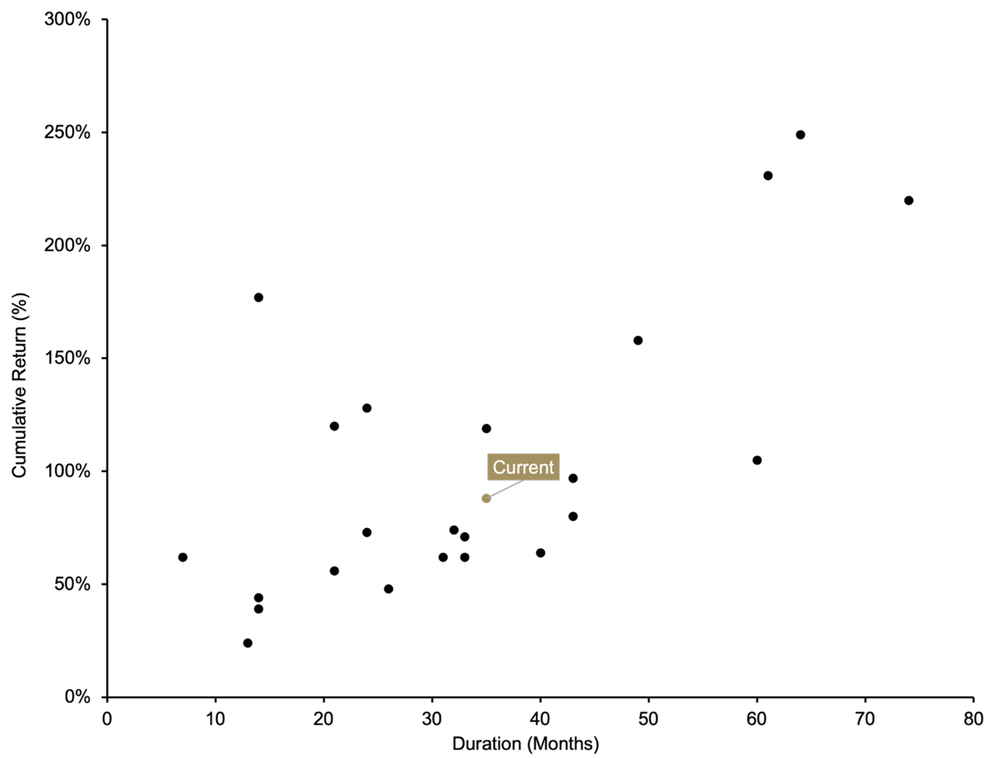
3. The Rally May Have More Room to Run

With equity markets near all-time highs, many investors are wondering if the current rally has run its course, and if it is time to lower their equity exposure and look for other options. If we look at the current bull market compared to previous advances, we can see that the duration of, and returns from, the recent bull run are near historical averages—but remain well below those of previous advances.

Figure 3. Size and Duration of Current Bull Run Relative to Other Rallies Suggest Possibility of Additional Upside

S&P 500 bull market cycles since 1928

Bull Cycle	Duration (Months)	Return
2009-2015	74	220%
1994-2000	64	249%
1982-1987	61	231%
2002-2007	60	105%
1942-1946	49	158%
1962-1966	43	80%
1949-1953	43	97%
1990-1994	40	64%
1953-1956	35	119%
Current	**35**	**88%**
1978-1980	33	62%
1987-1990	33	71%
1970-1973	32	74%
2016-2018	31	62%
1966-1968	26	48%
1935-1937	24	128%
1974-1976	24	73%
2020-2022	21	120%
1957-1959	21	56%
2018-2020	14	44%
1960-1961	14	39%
1932-1933	14	177%
1947-1948	13	24%
1938-1938	7	62%



Source: Oppenheimer & Co. and FactSet. Data as of 08/31/2025. **Past performance is not a reliable indicator or guarantee of future results.** For illustrative purposes only.

What does this imply? Simply put, based on historical experience, the current rally may have more fuel left in the tank.

Summing Up

As we have noted elsewhere, the key factors supporting the equity market remain positive. While risks exist, it is essential to keep the big picture in mind. Global economic growth is solid, driven by booming secular forces like generative artificial intelligence (AI), leading to resilient growth in corporate earnings. These powerful forces dominate market performance in the long run. We are also focused on quality stocks—those with long-term histories of robust earnings and steady dividend growth. We are also seeing potentially attractive opportunities in equity markets outside the United States, as the economic backdrop improves in many regions.

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Glossary & Index Definitions

Bullish refers to an optimistic outlook and to a belief that certain investments may potentially increase in value in the future. **Bull market** refers to a time when stock prices are rising, and market sentiment is optimistic. Generally, a bull market occurs when there is a rise of 20% or more in a broad market index over at least a two-month period. **Bearish** refers to a pessimistic outlook and generally refers to a belief that certain investment prices may fall in the future. **Bear market** refers to a time when stock prices are declining, and market sentiment is pessimistic. Generally, a bear market occurs when a broad market index falls by 20% or more over at least a two-month period.

Forward price-to-earnings ratio: Stock analysts calculate a forward price-to-earnings (P/E) ratio by dividing a stock's current price by estimated future earnings per share. Some forward P/Es are calculated based on estimated earnings for the next four quarters, while others use actual earnings from the past two quarters with estimated earnings for the next two. A forward P/E may help you evaluate the current price of a stock in relation to what you can reasonably expect to happen in the near future. In contrast, a trailing P/E is based exclusively on past performance.

Free cash flow margin is a financial metric that measures a company's ability to generate cash from its operations relative to its revenue. It represents a company's operating cash flow minus its capital expenditures in a specified period, expressed as a percentage of revenue.

Generative artificial intelligence (AI) focuses on creating new information based on inputs learned from existing data.

Momentum is an investment strategy that focuses on buying stocks that are outperforming and selling those that are underperforming.

The **S&P 500® Index** is widely regarded as the standard for measuring large cap U.S. stock market performance and includes a representative sample of leading companies in leading industries.

Indexes are unmanaged, do not reflect the deduction of fees or expenses, and are not available for direct investment.

Important Information