

MARKET SIGHT LINES



Third Quarter Earnings: Signs of Trouble or Resilience?

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Recently, we talked about [steps to take in a resilient market](#) before a market pullback. In the past, disappointing stock earnings, or learnings from earnings, have sometimes triggered market volatility and related pullbacks. And we're in the third quarter earnings season, with investors watching results carefully. We'll learn about things like the consumer – a key part of the economy – as well as the credit markets more broadly, where cracks can signal economic trouble. In this Sight|Lines, we discuss what investors are looking for – and seeing – as the third quarter earnings season unfolds.

THE TAKEAWAY: AGAINST A RESILIENT BACKDROP, EARNINGS WILL PROVIDE INSIGHTS ON WHERE WE'RE HEADED

As we enjoy a resilient market and economy, the third quarter earnings season should help us understand of such resilience will continue. In summary:

- Earnings are expected to grow this quarter and in 2025/2026, supporting profit margins.
- 12% of S&P 500 companies have reported so far, with many companies beating expectations.
- Early reports from the big banks signaled optimism about the current environment.
- Results by sector have varied so far, with Information Technology and Financials positing the most positive results, and Energy and Consumer Discretionary the most negative.
- Artificial intelligence (AI) results remain in keen focus, most especially with tech companies and hyper scalers.
- When looking for cracks, we'll watch to see if companies can maintain pricing power and raise prices if costs increase or if profit margins come under pressure.
- Many believe that stresses in the credit market can be an early sign of economic and market troubles, and some cracks with regional banks have spooked investors.
- It's notable that the positive performance of big tech companies is anchored on current earnings growth more than increasing optimism about future earnings growth.

IN-DEPTH: AGAINST A RESILIENT BACKDROP, EARNINGS RESULTS WILL HELP US BETTER UNDERSTAND WHERE WE'RE HEADED FROM HERE

Investors have benefitted from a resilient economy and market, but the third quarter earnings season may show signs of cracks in that resilience. Going deeper:

- Consensus earnings growth for this quarter and 2025/2026 remains positive, supporting profit margins:
 - The third quarter consensus earnings growth is now 8.5% year-over-year.
 - Full year consensus earnings growth for 2025 and 2026 are now 11% and 14%, respectively.
- 12% of S&P 500 companies have released earnings, with aggregate results leaning positive:
 - 86% of the companies have beat expectations.
- Reporting early in the season, the big banks had positive results and commentary:
 - These companies mostly beat expectations, with positive results in the areas of consumer banking and capital markets activity.
 - Company leaders indicated the economy remains robust and the consumer engaged.
- As is often the case, results have varied by sector:
 - Information Technology and Financials are leading with earnings growth of 31% and 22%, while Energy and Consumer Discretionary lagged with declines of 18% and 11%, respectively.
- Given the impact AI on our economy and the prospect for more, tech company results, especially hyper scalers, are in focus:
 - The “Magnificent Seven” are expected to post 14.9% year-over-year earnings growth in Q3 2025.
- Companies’ abilities to maintain pricing power (increase prices if costs rise) will be in focus:
 - At present, profit margins are forecast to remain flat at 12.8%, inferring that pricing power will be maintained. We’ll be watching to see if margins come under pressure.
- Observers are watching for credit market cracks as a leading indicator of economic and market troubles:
 - Two regional banks disclosed bad loans tied to alleged fraud.
 - When reporting a credit loss, one CEO said, “when you see one cockroach, there's probably more.”
- Notably, the positive performance of the “Magnificent Seven” companies is anchored on current earnings growth:
 - So far in 2025, the majority of the Magnificent Seven’s total return has been due to earnings growth rather than an expansion in price-earnings ratio, a move sometimes associated with increased optimism about future earnings.

CONCLUSION

In the past, disappointing stock earnings, or even insights from earnings, have sometimes served as a catalyst for market pullbacks. Since we recently discussed [steps to take in a resilient market](#) before a pullback, we’re watching third quarter earnings season closely. As companies report, we’ll get a good sense for how the consumer is holding up, and important player in the economy. And we’ll also learn about the credit markets, an important focus where cracks can be a precursor for trouble. The economy and markets have been resilient. But we must be ready for a pause in that resilience.

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