S&P 500 Checkup
4/14/2017

Fundamentals

	YOY growth in the sum total	Median yoy growth
Revenue	2.0%	1.8%
EBITDA	6.7%	9.4%
Operating income	-0.2%	4.5%
Operating Cash Flow (OCF)	-4.1%	6.7%
EBITDA margin	15.3%	
OI margin	13.1%	

Capital allocation

	YOY growth in the sum total	%OCF
Capital expenditures	-5.0%	35.6%
Dividends	7.0%	26.4%
Share repurchases	-0.2%	32.2%
R&D spending	6.6%	13.6%

Warning flags	YOY growth in the sum total	Number of companies with yoy increase
Net debt (Debt - cash)	6.7%	265
Share based compensation	11.4%	235
		Number of companies
Goodwill writedowns	-73.2%	39
Extraordinary items	-31.3%	215

S&P 500 Checkup
Glossary and Commentary

Notes
The S&P 500 is comprised of constituent companies as of the date of the report for all periods.

Fundamentals give an indication of the economic health of the S&P 500 as a whole. Some of the things we look for are revenue growth that corroborates GDP expectations and indications of where operating earnings are heading.

Areté's take: In aggregate, revenue growth corroborates low single digit GDP growth, although declining income and cash flow suggests corporate profitability may finally be peaking after many years of growth.

Capital allocation identifies the key uses of capital. This is useful because capital that is reinvested in the business through capital expenditures and R&D will provide a solid foundation for future growth. Capital that is returned to shareholders diminishes a company's capacity for future growth.

Areté's take: With capital spending down yoy and R&D only partially offsetting it, aggregate reinvestment is muted. This is corroborated by the fact that over 50% of operating cash flow is being returned to shareholders though dividends and share repurchases, and therefore not invested for future growth.

Warning flags comprise a number of measures that can highlight potential problems before they become evident in other numbers. Net debt increases risk if it rises faster than the income to service it. Share based compensation is a real expense that often gets overlooked or excluded from presentations. Goodwill writedowns are normally indications of past acquisitions that did not work out and reflect on both industry conditions and management quality. Extraordinary items can help (or hinder) the analysis of underlying operating trends.

Areté's take: Aggregate net debt continues to increase faster than aggregate cash flows which reflects incremental leveraging of S&P 500 company balance sheets while rates are low. There was a significant decline in the dollar value of goodwill writedowns although the prior year was dominated by unusual multi-billion dollar writedowns at GE, MSFT and YHOO.

Overall view: We continue to see modest erosion in the overall financial health of S&P 500 companies in aggregate. Normally this would merit only modest caution, but in the context of extremely high valuations, it increases the likelihood that companies will disappoint high expectations.

For questions and comments, please send an email with your name to: info@areteam.com.

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