Yardeni Research

November 5, 2025

Morning Briefing

On AI & Earnings

Check out the accompanying chart collection.

Executive Summary: The first wave of AI adoption was about making work more efficient. The coming wave will be about redesigning work itself, says Melissa. AI is likely to transform the labor force by eliminating humans' grunt work and creating new human-in-the-loop roles. … Also: Joe reports that Q3 earnings season is looking like one for the record books: The S&P 500 companies that have reported to date collectively have record-high EPS and double-digit y/y earnings growth. Plus, they're collectively beating estimates by more than 10%.

AI: Useful Across All Sectors. Artificial intelligence (AI) isn't the future anymore—it's currently utilized by companies across all S&P 500 sectors. It's helping humans to write code, produce creative content, improve medicine, prevent fraud, maximize capacity, design spaces, and much else.

The current wave of AI aims to help companies and workers to become more efficient. The fast-approaching next wave will be about reinvention: Systems won't just automate work processes but revamp them. AI won't supplant HI (Human Intelligence) but augment it. When the two types of intelligence learn to collaborate for optimal productivity, it will supercharge profitability growth across all sectors.

Below, we explore just some of the ways that AI use is proliferating across sectors and share a few thoughts on where AI use could develop in the future:

(1) *Technology.* Use of AI is spreading the fastest among tech companies. AI code-generation tools now handle a sizable share of everyday programming, lifting developer output.

One large-scale academic *study* observed a 28% increase in code shipment volume through an in-house AI platform that combines code generation and automated review capabilities into programmers' daily workflows.

Early chip designers spent nearly 40% of their time on compiling information and manual interventions. Now, several electronic design automation (EDA) vendors, *including* Synopsys, offer AI-infused tools that promise to automate fact-finding and manual interventions. That's enhancing productivity by freeing up designers' time to develop more complex chips with greater capabilities.

The next tech wave, "agentic" AI and local (versus cloud-based) AI computation, has arrived. Agentic AI tools enable dynamic enterprise systems to *rewrite* their own workflows in real time. Local on-device AI is rapidly gaining traction as companies shift away from cloud-only models. Nvidia's *DGX Spark*, a $4,000 compact workstation capable of 1,000 trillion operations per second for local model training and inference, exemplifies this trend.

(2) *Communication services.* AI is influencing what we watch, see, and hear online. It is well known that AI-powered algorithms influence viewing activity on social media. Advertising is now an algorithmic science. Machine-learning models constantly refine audience targeting, improving engagement rates. PwC expects that generative AI programs will not only curate but also *create* an increasing share of dynamic, personalized digital advertising.

(3) *Consumer sector.* Retailers are *trimming* inventory costs by improving stock levels, thanks to predictive AI demand systems. Coming soon: *dynamic AI smart packaging*—labels that adjust prices or freshness data in real time—and *AI generated fulfilment*, where warehouse systems forecast orders, pre-position goods, and even generate shipping routes automatically.

(4) *Health care.* This is an area ripe for AI transformation. The amount of time it takes to discover and develop pharmaceuticals is decreasing as AI algorithms *identify* promising molecules that are now entering trials. AI-empowered diagnostic tools can *rival* radiologists in spotting specific conditions on ultrasounds and other scans. Over time, expect AI to enable *personalized medicine* tuned to each patient's biology, *predictive health modeling* for early-stage intervention, and *surgical systems* that handle routine steps while humans focus on judgment calls.

(5) *Finance.* The financial services industry embraced AI early because it stood to benefit from immediate and direct impacts on profits. AI-powered *fraud detection* in financial services has reached accuracy rates of around 95%. More global equity trading volume is now *executed* via AI-driven algorithms than ever before. The next phase of AI adoption will enable continuous *stress testing*, *automated compliance*, and *digital advisors* that mimic human reasoning.

(6) *Industrials and materials.* While *predictive maintenance* has existed for years, AI is making it far more precise—processing sensor data at scale to detect micro-anomalies and predict failures days or weeks earlier. Future systems may feature autonomous factories running on self-learning programs to maximize capacity.

(7) *Energy and utilities.* AI already predicts equipment failures and interprets seismic data, but its biggest potential lies in *grid management*. Traditional systems match supply and demand through pre-set schedules and operator judgment; AI models process millions of *real-time* inputs—weather, consumption spikes—and instantly reallocate power or storage. The result: fewer outages and a more efficient use of every megawatt.

(8) *Real estate.* The real estate industry has been slow to adopt AI, but it's catching up fast. AI-powered *valuation models* aren't replacing appraisers outright—but they're narrowing the gap between speed and accuracy. Generative tools can be used by agents, brokers, and developers to create *virtual staging* of homes and commercial spaces in seconds—swapping furniture styles, lighting, or even floor plans to match buyer preferences. The next frontier is design: AI that tests thousands of *building layouts* to optimize for cost, sustainability, and livability. Eventually, *self-managing buildings* could learn from occupants and negotiate energy use directly with the grid.

Our bottom line: AI is likely to transform the labor force by eliminating grunt work for humans and *creating* new human-in-the-loop roles, such as AI-product developers, AI-compliance technicians, AI-data analysts, and AI-ethics specialists.

Strategy: Q3 Earnings Season Is Among the Best Ever! With 72% of the S&P 500 companies having reported September-quarter results through mid-day Tuesday, we have a pretty good handle on how strong the quarter was for these companies.

So far, their aggregate "blended" quarterly EPS—a mix of actual EPS for companies that have reported Q3 and consensus estimates for those that haven't—is $70.65 (*Fig. 1*). That's up 6.0% q/q from its record-high $66.68 in Q2 (see our *web pub* *S&P 500 Quarterly Metrics*).

The degree to which Q3 earnings beat analysts' expectations improved q/q to a 16-quarter high of 10.5% (*Fig. 2*). That earnings surprise (measured as the change in actual reported EPS from the consensus Q3 mean at the time of each company's report) is up notably from Q2's 8.2% beat, is the strongest since Q3-2021, and ranks 10th best among beats in the 155 earnings seasons since Q1-1987.

Also up: Q3's blended EPS relative to analysts' expectations at the end of September, before reporting season began; at that point, their consensus estimates implied record-high EPS of $67.24 and a y/y growth forecast of just 6.4% (*Fig. 3*).

As for Q3's y/y growth percentage, it has been in the double digits for four straight quarters and in five of the last six quarters. With 28% of the companies left to report, the S&P 500's unpublished blended y/y earnings growth rate for Q3 is 11.8%, up from 10.4% last week. That marks the ninth straight quarter of positive y/y earnings growth, the longest string since 12 straight quarters through Q2-2019 (*Fig. 4*).

However, Q3's y/y growth rate remains in the low double-digit percentages and is down from Q4-2024's 13.7% y/y (a 12-quarter high) (*Fig. 5*). On a proforma same-company basis, S&P 500 blended earnings rose 13.8% y/y in Q3, marking a ninth quarter of such growth (about matching H1-2025's rate, but down from 17.1% in Q4-2024).

Here's more, courtesy of Joe:

(1) *More sectors outperform S&P 500's Q3 earnings growth.* Ten of the 11 S&P 500 sectors have been delivering rising earnings y/y so far in Q3, and five are ahead of the overall S&P 500's y/y growth rate. If the Energy sector finishes Q3 with y/y earnings growth too (and it has a good shot), all 11 sectors will be y/y growers for the first time since Q4-2021.

Five sectors are recording double-digit percentage y/y earnings growth in Q3, up from three in Q2 and way down from seven in Q4-2024. Among Q3's laggards, Energy's earnings are down 3.7% y/y (way better than its double-digit-percentage declines in eight of the prior nine quarters). On a positive note, Information Technology's earnings growth was in double digits for a ninth straight quarter and Communication Services' for a fifth.

Here's how the sectors' y/y earnings growth has stacked up so far on a proforma basis: Information Technology (25.3%), Real Estate (22.2), Financials (22.0), Communication Services (16.8), Materials (14.8), S&P 500 (13.8), Consumer Discretionary (9.2), Industrials (8.2), Utilities (2.0), Health Care (1.6), Consumer Staples (0.3), and Energy (-3.7).

(2) *Magnificent-7.* Through midday-Tuesday, Nvidia is the only Mag-7 that hasn't yet reported September-quarter results. The "Magnificent-6's" aggregate Q3 earnings surprise was 16.2%, and its y/y earnings growth of 26.8% was nearly triple the consensus' 9.1% forecast—all well above the S&P 500's measures (*Fig. 6*).

Only three of the six had double-digit percentage earnings surprises, but five had double-digit y/y earnings growth: Amazon (24.0% earnings surprise, 36.4% y/y earnings growth), Meta (8.4, 20.2), Apple (4.4, 12.8), Microsoft (12.7, 25.2), Alphabet (33.3, 46.2), and Tesla (-8.7, -30.6).

(3) *Stronger Q3 for S&P 493*. The S&P 493's y/y growth rate has eased to 9.1% y/y in Q3 from a 12-quarter high of 13.2% in Q4-2024. But the group's total earnings rose to a new record high again in Q3 and beat consensus forecasts by a healthy 8.5%.

Calendars

US: Wed: ADP Employment 28K; ISM NM-PMI 51.0; S&P Global C-PMI & NM-PMI 54.8, 55.2; MBA Mortgage Applications; Bowman. **Thurs:** Williams; Bowman; Waller. (Source: FX Street)

Global: Wed: Eurozone, Germany & France C-PMIs 52.2, 53.8 & 46.8; Eurozone, Germany & France NM-PMI 52.6, 54.5 & 47.1; Eurozone PPI -0.1%m/m, -0.2%y/y; Germany Factory Orders 1.2%; UK C-PMI & NM-PMI 51.1 & 51.1; China Caixin NM-PMI 52.6; Lagarde; Balz; Breeden. **Thurs:** Eurozone Retail Sales 0.2%m/m, 1.0%y/y; Germany Industrial Production 3.0%; BoE Interest Decision 4.0%; Nagel; Villeroy; De Guindos; Schnabel; Bailey; Paulson. (Source: FX Street)

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