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These Growth Stocks Are Looking Up

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Many investors are increasingly convinced that the worst of the recession is behind us. Although optimism about future growth has pushed share prices up fairly dramatically since earlier this year, it's taken awhile for that optimism to translate into higher expectations for company earnings.

Slow on the uptake
That delayed reaction is nothing new for growth stocks. When the recession first hit, many high-growth companies didn't immediately face up to the prospects of falling earnings and revenue growth rates. Given the way their stocks had performed throughout the previous bull market, investors hoped that those companies would stay resilient and buck the trend with sustained growth. As a result, it was easy to stay in a state of denial about just how bad the market meltdown would be -- at least until companies started reporting actual results that shellshocked shareholders simply couldn't ignore.

Similarly, after the market's lows in March, investors weren't necessarily in any hurry to think about an earnings recovery, even as share prices started to rebound quickly. Having gotten burned by companies that didn't hold up as well during the recession as they had hoped, investors were conservative in their expectations.

Now that many companies have reported a couple of quarters of decent results, however, analysts are finally getting around to marking up their guesses on future earnings. Just take a look at how much forward estimates for some companies have risen in just the past 90 days:

Stock	Forward EPS Estimate 90 Days Ago	Current Forward EPS Estimate	Change
Priceline.com (Nasdaq: PCLN)	7.43	8.97	20.7%
Apple (Nasdaq: AAPL)	7.88	9.35	18.7%
Google (Nasdaq: GOOG)	24.59	26.29	6.9%
Intel (Nasdaq: INTC)	1.10	1.46	32.7%
Baidu (Nasdaq: BIDU)	8.38	9.28	10.7%
BHP Billiton (NYSE: BHP)	2.96	4.02	35.8%
Ebix (Nasdaq: EBIX)	3.16	3.63	14.9%

Source: Yahoo! Finance. Forward estimates are for the next fiscal year.

In most of these cases, rising estimates are only putting these companies' profits back in line with their longer-term expected trends. Notice how their expected near-term earnings growth now compares with five-year estimates:

Stock	Expected Earnings Growth This Year	Expected Earnings Growth Next Year	Expected 5-Year Earnings Growth

Priceline.com	25%	19.8%	18%
Apple	9%	16.8%	18%
Google	16.5%	15.8%	20.1%
Intel	(13%)	82.5%	11%
Baidu	41%	49.9%	39.8%
BHP Billiton	52.6%	24.8%	(9.8%)
Ebix	28.5%	23.9%	17.5%

Source: Yahoo! Finance.

You can see how with the exception of BHP Billiton, which analysts apparently see more as a cyclical play on commodities than as a true growth stock, most of these stocks have a similar appearance here. Only now that analysts have boosted their earnings estimates do these stocks have a chance to offer growth rates for next year that match up at least fairly closely with their long-term earnings growth.

That helps to explain why many of these stocks have rallied this year. During the worst of the crisis, no one knew if a struggling economy would knock growth stocks off their upward trajectories permanently. At least for now, though, analysts are treating 2008 as an anomalous blip, forecasting a return to rosier times for these growth stocks.

Keep your eyes open
The danger, though, is that after a big run-up in the stock market, growth stocks now need those rosy scenarios actually to play out. Now that expectations are much higher, even a relatively small miss could send stocks over a cliff fairly quickly. Moreover, given how notoriously inaccurate long-term earnings forecasts are, there's no guarantee that stocks can keep up this pace that long.

Rather than relying solely on Wall Street analysts, you should have your own opinion of where you see a company's future earnings going. That way, you'll know what *you* expect, and it'll be much easier to decide what to do next based on how the future plays out for these and the other growth stocks in your portfolio.

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