“Stocks look cheap relative to corporate profits” by at least one barometer of U.S. shares, according to James W. Paulsen, Wells Capital Management Inc.’s chief investment strategist.

The CHART OF THE DAY shows his gauge: the ratio of the Standard & Poor’s 500 Index to after-tax earnings for all U.S. companies, as compiled quarterly by the Commerce Department, in billions of dollars.

Since 1947, the S&P 500 has averaged 1.3 times profit on this basis. The ratio at the end of this year’s first quarter, the most recent period for which earnings are available, was 1.08. Yesterday’s close for the index equaled 1.12 times the first-quarter total.

“The stock market may still have considerable potential” based on this comparison, Paulsen wrote in a report three days ago. Prices are no higher than they were in 1952 and 1985 amid bull markets, the Minneapolis-based strategist wrote.

The S&P 500 rose to more than three times the earnings figure in 2000’s first quarter, when a 1990s advance driven by Internet stocks ended. Conversely, the
ratio was only about 1.2 as five years of gains concluded in the fourth quarter of 2007.

In the next several years, shares are headed for annual returns of 10 percent or more, Paulsen wrote in a follow-up e-mail. The S&P 500-to-earnings indicator shows they “may be much cheaper than most think.”

To contact the reporter on this story: David Wilson in New York at dwilson@bloomberg.net

To contact the editors responsible for this story: Chris Nagi at chrisnagi@bloomberg.net Michael P. Regan, Jeremy Herron