**MORNING BRIEFING**
**August 19, 2021**

## Retail, Earnings & Carbon

*Check out the accompanying chart collection.*

(1) Consumers spending differently now. (2) Sweatpants are out, notebooks and pencils are in. (3) Target beats analysts' target. (4) Lowe's CEO still upbeat on housing. (5) TJX customers back to bargain shopping. (6) Analysts defy Delta and raise earnings forecasts. (7) Hoping carbon-capture technology can save the world. (8) The oil giants enter the carbon-capture game. (9) Gathering carbon from the air, chimneys, and tailpipes. (10) Turning captured CO2 back into fuel.

**Consumer Discretionary: Retailing Tales.** The strength of US consumer spending last year despite waves of Covid-19 illness and death was truly amazing. The Internet, the advent of curbside pickup, and plentiful government subsidies allowed consumer spending to surge in 2020 outside of a brief two-month span (*Fig. 1*). Now that Covid-related deaths remain low and the unemployment rate has fallen to 5.4%, consumers have changed what they're buying, but they're still out shopping.

July's retail sales fell 1.1% from June's level, but they were hurt by the 3.9% drop in auto sales, as dealerships struggle with a lack of inventory thanks to the semiconductor chip shortage. Retail sales excluding motor vehicles dropped 0.4% last month (*Fig. 2*). Meanwhile, retailing giants Walmart, Target, Home Depot, Lowe's, and TJX all showed continued sales gains in Q2, and none warned that August sales showed signs of slowing down.

Let's take a look at what a few retailing CEOs had to say on recent conference calls:

(1) *Hitting the bullseye.* Target's Q2 comparable-store sales jumped 8.9% y/y, off a Q2-2020 base that itself saw sales growth of 24.2%. Adjusted earnings jumped almost 8% to $3.64 per share in the quarter, beating analysts' estimate of $3.51 a share.

While CEO Brian Cornell acknowledged the potential for volatility in H2 due to the uncertainty of the Delta variant, Target nonetheless increased its H2 forecast slightly. It now expects comparable sales growth in the high-single-digit range, compared to the single-digit comp growth it forecast during the Q1 earnings conference call. "[W]e're seeing tremendous resilience in the consumer today and in our traffic patterns," said Cornell.

Target executives described back-to-school sales as “really strong” and “broad based.” There has been less buying of household essentials and more buying of dresses and beauty products. Sporting goods enjoyed high-teens sales growth, while electronics sales fell in the mid-single-digit range because last year some of Target’s electronics competitors were closed.

(2) *Lowe’s: Building on success.* The home retailer is undoubtedly facing tough comparisons to last year when DIY projects gave us something to do while trapped at home. Total sales edged up only 1.1% in Q2, and comparable sales in the US fell 2.2%.

Nonetheless, Lowe’s increased its full-year outlook and now expects 2021 revenue of $92 billion, up from the $86 billion it expected in May and prior guidance of $84 billion. If the company hits its 2021 target, it would mark an increase from 2020’s sales of $89.6 billion, which was a 24.2% jump from 2019’s results.

CEO Marvin Ellison spoke very positively about the US housing market, citing historically low mortgage rates, demand that’s exceeding supply, and rising prices. “[B]ecause of this, consumers have an increased confidence in repairing and remodeling their homes.” That’s good news for Lowe’s because two thirds of the company’s sales are generated from home repair and maintenance activity.

(3) *Consumers love bargain hunting.* TJX stores were largely closed in Q2 last year, and the company has little in the way of e-commerce sales. So unlike for many other retailers, TJX’s Q2-2021 comparisons were easy. Q2 sales jumped 23% y/y to $12.1 billion, even though some of the company’s stores are currently closed in Australia.

CFO Scott Goldenberg described robust Q3 sales so far: “[W]e are very pleased that overall open-only, comp-store sales trends are up very strongly to start the quarter at the mid-teens level.” The company isn’t providing guidance for Q3 or H2.

**Strategy: Earnings Forecasts Still on the Rise.** If you’re looking for a reason to remain positive despite the stock market selloff, consider analysts’ forward earnings estimates, which continue their upward trend. “Forward earnings” is the time-weighted average of consensus earnings-per-share estimates for this year and next; it’s a more precise rendering of the projected earnings that investors actually are basing decisions upon than analysts’ estimates for full years or quarters.

Over the past four weeks, the S&P 500’s forward earnings have increased by 3.8%, and over the past 13 weeks, the change is 7.7%. Here's a quick look at which S&P 500 industries' forward earnings have been revised by the most and the least over the past four weeks (for full details, see our *S&P 500 Sectors & Industries Forward Earnings & Revenues*):

(1) *Acting like Covid has passed.* The third wave of Covid-19 continues to take a toll, particularly on the unvaccinated. The number of new cases, using a seven-day average, topped 125,000 this week, up sharply from 12,000 in June (*Fig. 3*). But so far, the number of deaths remains relatively low compared to the January peak (*Fig. 4*).

Analysts aren't panicking—yet. They continue to boost the forward earnings of industries that will be hurt if consumers start staying home for fear of catching Covid. Here's how earnings have changed over the past four weeks for some of the S&P 500 industries related to economic reopening: Hotels (60.5%), Casinos & Gaming (24.4), Restaurants (4.9), and Movies & Entertainment (3.7).

(2) *Oil is down, but oil-related earnings aren't.* The price of Brent crude oil futures has fallen 10.5% from its high on July 5 through Tuesday's close, though is still up 52% y/y (*Fig. 5*). The recent decline is attributed to recent signs of an economic slowdown in China and rising Covid-19 cases around the world. But so far, analysts' confidence in the sector's earnings power continues to grow.

Looking at the four-week percentage changes in forward earnings of the S&P 500 and all 11 of its sectors, it's notable that every single one is a positive change, with Energy leading the pack: Energy (10.8%), Real Estate (8.7), Communications Services (7.3), Industrials (5.4), Materials (5.1), Information Technology (4.0), S&P 500 (3.8), Consumer Discretionary (2.8), Health Care (2.5), Financials (1.6), Consumer Staples (0.8), and Utilities (0.5).

Within the Energy sector, earnings estimates have risen over the past four weeks for Oil Exploration & Production (15.8%), Oil & Gas Equipment & Services (12.1), and Integrated Oil & Gas (9.8).

A number of industries typically associated with US economic health also have benefitted from positive earnings estimate revisions over the past four weeks, including: Specialty Stores (21.4%), Human Resources & Services (18.5), Home Furnishings (8.6), Consumer Finance (8.1), Steel (7.8), Automobile Manufacturers (7.4), Apparel & Accessories (6.6), Homebuilding (5.6), Trucking (5.1), Semiconductor Equipment (4.7), Advertising (4.2), and Railroads (3.5).

(3) *Not much negative to tell.* There's not much negative in this snapshot of earnings revisions over the past four weeks. Only seven industries have seen their earnings revised downward over the past four weeks. Those industries include Broadcasting (-0.2%), Gold (-0.8), Diversified Banks (-1.0), Household Products (-1.3), Internet & Direct Marketing Retail (-4.6), Alternative Carriers (-4.8), and Apparel Retail (-5.9).

Internet and Direct Marketing Retail is home to Amazon, for which analysts have been shaving their earnings forecasts recently. They now expect the company's 2021 earnings to be $53.13 a share, down from $55.84 one month ago, and its 2022 earnings to come in at $67.40 a share, down from $73.22 a month ago, according to the *WSJ*. The share price performance of the Internet retailing giant turned negative ytd as of Tuesday's close (-0.5%), underperforming the S&P 500's 18.4% ytd gain.

**Disruptive Technologies: Capturing Carbon.** On August 9, the United Nations' (UN) Intergovernmental Panel on Climate Change (IPCC) issued its Sixth Assessment Report (AR6), titled *Climate Change 2021*. UN Secretary-General António Guterres described the report as "a code red for humanity." Guterres added, "The alarm bells are deafening, and the evidence is irrefutable: greenhouse gas emissions from fossil fuel burning and deforestation are choking our planet and putting billions of people at immediate risk." In just the last few weeks, floods have wreaked havoc in Europe, China, and India; toxic smoke plumes have blanketed Siberia; and wildfires have burned out of control in the US, Canada, Greece, and Turkey.

President Joe Biden has pledged to reduce US greenhouse gas emissions by at least 50% by 2030. So far, he has announced plans to increase the fuel efficiency of cars, and his $1 trillion infrastructure bill contains lots of funding to improve the electrical grid and energy production. The legislation earmarks about $7.5 billion for building electric vehicle charging stations and $7.5 billion to replace carbon-spewing school buses and ferries with lower-emissions vehicles. There's growing bipartisan support for a separate proposal of placing a carbon tax on companies that produce greenhouse gases and carbon dioxide ($CO_2$). Proceeds from the tax would be invested in clean energy solutions.

However, the IPCC had a decidedly doomsdayish spin, concluding, "Many changes due to past and future greenhouse gas emissions are irreversible for centuries to millennia, especially changes in the ocean, ice sheets and global sea level." I asked Jackie to see if there might be technological solutions to this problem. After all, technology has a long history of averting doomsday scenarios such as population explosions, global famine, and more recently pandemics (notwithstanding the obvious counterexample of the atom bomb).

Here is her report:

Many experts say that companies—particularly those in industries like steel and concrete manufacturing—will need to adopt technologies that are able to capture the carbon thrown off by their manufacturing processes. Carbon-capture technology is a quickly evolving area, with small and large energy companies trying to invent ways to capture large volumes of carbon from the air at a reasonable price. Companies that succeed might apply for the Xprize, the $100 million worth of prizes that Elon Musk will award to those with the best ideas.

Critics of carbon-capture technology argue that it encourages companies to continue producing CO2 and it is an inefficient way to clean the atmosphere. The critics would prefer that CO2 not be created at all or be extracted from the air by planting trees.

(1) *Don't pump oil, capture carbon.* Not surprisingly, some of the largest companies focused on developing carbon-capture technology are the oil and gas giants. Exxon Mobil is investing $3 billion through 2025 in a business unit formed this year that focuses on low-carbon solutions. The new business will capture CO2 emissions from industrial processes as well as directly from the air and deposit it underground, a February 1 *WSJ* *article* reported.

In March, Shell, Total SE, and Equinor AS launched a joint venture to capture carbon and store it thousands of feet beneath the sea off the coast of Norway. The Northern Lights project, scheduled to start in 2024 and largely funded by Norway, counts as customers Fortum Oslo Varme, a waste company, and HeidelbergCement AG. The joint venture marks the first time that companies outside of the oil industry would pay to have their carbon captured and stored, an April 19 *WSJ* *article* reported.

But there are concerns about CO2 escaping during the intricate processes, which involve collecting the CO2, shipping it, pumping it offshore, and injecting it into an aquifer under the seabed.

Like other energy giants, Chevron and BP are developing carbon-capture projects in the hopes of their becoming profits-producing businesses. Their bottom lines will be helped by tax credits from countries around the world. "The U.S. offers companies a tax credit of as much as $50 a metric ton of carbon captured, while the U.K., Norway and Australia have collectively committed billions of dollars of funding for carbon-capture projects," the aforementioned April 19 *WSJ* article explained. A record 17 new carbon-capture projects were slated for development last year.

(2) *Capturing carbon on tailpipes.* The startup Remora has developed a device that attaches to the tailpipes of 18-wheelers to capture up to 80% of emitted CO2. The CO2 is compressed and stored in a tank that must be unloaded by the truck's driver into a stationary tank, where it's cooled and liquified. A tanker then pumps out the liquified CO2 to be sold for reuse, an August 9 *WSJ* *article* explained. Ryder Systems, Werner Enterprises, NFI Industries, ArcBest, and Cargill plan to test the new system.

(3) *Capturing CO2 from chimneys.* Companies are working on different ways to collect CO2 before it leaves an industrial plant's chimney and pollutes the air. Compact Membrane has a membrane that it *says* can capture the CO2 from gas exiting a factory's flue at a cost of $20 a ton, making it a cost-effective option.

Membrane Technology & Research also makes CO2-absorbing membranes that can reduce the CO2 produced by coal- or natural-gas-fired power plants and other industrial plants. And Carbon Clean has a carbon-capture solution that's installed in industrial plants' flues.

(4) *Building a better tree.* Carbon Collect has created the MechanicalTree, which takes CO2 out of the air that's blown past it by the wind. Because it uses the wind, it doesn't need to run fans or blowers at additional cost. The CO2 is pumped and stored underground or recycled and turned into a synthetic fuel for use by companies that produce products using CO2 (e.g., manufacturers of food and beverages, cement, concrete, steel, pharmaceuticals, carbon fiber, and fuels), the company's *website* explains. One cluster of 12 MechanicalTrees can capture 1 metric ton of CO2 per day.

(5) *Pulling CO2 out of thin air.* Carbon Engineering has two direct-air-capture plants that use large fans to pull air into a structure where it passes over a thin plastic surface covered with a potassium hydroxide solution, which chemically binds with the CO2 and removes it from the air. The CO2 in the solution undergoes a number of chemical processes that yield CO2 gas that can be used or buried. The company's *website* claims it can remove as much as one million tons of CO2 per year at a cost of about $100 per ton.

The company is working with LanzaTech (discussed below) to investigate the feasibility of a large-scale facility in the UK that would remove CO2 from the air and turn it into aviation fuel. If it moves ahead, the facility would be up and running by the end of the decade. British Airways and Virgin Atlantic are part of the project team, according to a July 26 *press* *release*.

Climeworks, a Swiss startup, also performs direct-air capture of $CO_2$. Fans pull air through a filter that attracts only $CO_2$. When the filter is saturated, it is heated to 100 degrees Celsius and pure $CO_2$ is released and collected. The $CO_2$ can be either buried or sold for other uses, a July 23 CNBC *article* explained. The company's plant in Switzerland removes about 900 tons of $CO_2$ per year, which it hopes to increase to several gigatons.

(6) *Recycling the carbon.* Instead of stuffing the $CO_2$ back into the ground, LanzaTech combines the captured gas with bacteria to make fuels and chemicals. It has two plants in China that capture $CO_2$ gas spewed by steel mills and convert it into ethanol for use in making various products—e.g., jet fuel, household cleaners, laundry detergent, perfumes, and polyester—according to a company *press release*.

## Calendars

**US: Thurs:** Leading Indicators 0.8%, Initial & Continuous Jobless Claims 365k/2.80m, Philadelphia Fed Manufacturing Index 23.0, Natural Gas Storage. **Fri:** Baker-Hughes Rig Count. (Bloomberg estimates)

**Global: Thurs:** Japan Core CPI -0,4% y/y, Kent. **Fri:** UK Headline & Core Retail Sales 6.0%/5.7% y/y, Canada Headline & Core Retail Sales 4.4%/4.6% y/y. (Bloomberg estimates)

## Strategy Indicators

**Stock Market Sentiment Indicators** (*link*): The Bull/Bear Ratio (BBR) sank below 3.00 for the first time since the week of March 16, falling for the second week to 2.76 after a three-week gain from 3.18 to 3.55. It was at 4.00 five weeks ago, which was the highest since late January 2018. Bullish sentiment dropped to 51.1% this week—the fewest bulls since early March's 51.0%—after increasing the prior two weeks from 52.6% to 56.4%. Meanwhile, bearish sentiment, which has fluctuated in a narrow band the past few months, jumped from 15.9% to 18.5% this week—the highest percentage since the March 23 week. In the meantime, the correction count climbed to 30.4% after falling from 30.9% to 27.7% the previous two weeks. The AAII Ratio advanced to 54.0% last week, after falling from 60.0% to 53.2% the week before, as bullish sentiment inched up from 36.1% to 37.0% and bearish sentiment edged down from 31.7% to 31.5%.

**S&P 500 Sectors Earnings, Revenues, Valuation & Margins** (*link*): Last week saw consensus forward revenues and earnings rise for nine of the 11 S&P 500 sectors. Forward revenues was higher for all but Financials, and earnings was higher for all but Consumer Discretionary and Industrials. Six sectors have both their forward revenues and earnings at or near record highs: Communication Services, Consumer Discretionary, Consumer Staples, Health Care, Information Technology, and Materials. Energy and Real Estate still have both measures below record highs. Industrials' forward revenues is poised to make a new high, but forward earnings is lagging. Financials and Utilities have forward earnings at or near record highs, but their forward revenues are lagging. Only three sectors posted a higher profit margin y/y in 2020: Consumer Staples, Tech, and Utilities. For 2021, a y/y improvement is expected for all but Utilities now, as Real Estate turned the corner in the latest week. The forward profit margin was at record highs during 2018 for 8/11 sectors, all but Energy, Health Care, and Real Estate. Currently, five sectors are at record highs. Here's how they rank based on their current forward profit margin forecasts versus their highs during 2018: Information Technology (24.8%, record high), Financials (19.8, a new record high this week), Communication Services (16.7, record high), Real Estate (16.3, down from 17.0), Utilities (14.4, down from its 14.8 record high in early May), Materials (13.2, record high), S&P 500 (13.2, record high), Health Care (11.0, down from 11.2), Industrials (10.0, down from its record high of 10.5% in mid-December), Consumer Staples (7.6, 7.7), Consumer Discretionary (7.8, down from 8.3), and Energy (7.4, down from 8.0).

**S&P 500 Earnings, Revenues, Valuation & Margins** (*link*): The S&P 500's forward profit margin remained steady last week at a record high of 13.2%. Since the end of April, it has exceeded its prior record high of 12.4% in September 2018. It's now up 2.9ppts from 10.3% during April 2020, which was the lowest level since August 2013. Forward revenues and earnings per share both rose w/w. They've both been making new record highs since the beginning of March and for the first time since February 2020. Since the Q2-2020 earnings season came in way better than expected, analysts have been playing catch-up with their lowball estimates from the Covid-19 shutdown. Consensus S&P 500 forecasts had been falling at rates paralleling the declines during the 2008-09 financial crisis. Forward revenues growth rose 0.1ppt w/w to 8.9%. That's down from a record high of 9.6% at the end of May and should continue to move lower due to base effects. Still, that's up from 0.2% during April 2020, which was the lowest reading since June 2009. Forward earnings growth remained steady w/w at 17.2%, but should also continue to move lower due to base effects.

That's down from its 23.9% reading at the end of April, which had been its highest since June 2010 and up substantially from its record low of -5.6% at the end of April 2020. On a positive note, analysts continue to raise their 2021 forecasts for revenues and earnings growth and the profit margin. They now expect revenues to rise 14.7% in 2021 (up 0.3ppts w/w) and 6.6% (unchanged w/w) in 2022 compared to the 2.1% decline reported in 2020. They expect earnings gains of 45.4% in 2021 (up 0.4ppts w/w) and 9.1% in 2022 (down 0.1ppt w/w) compared to a 13.3% decline in 2020. Analysts expect the profit margin to rise 2.7ppts y/y in 2021 to 13.0% (up 0.1pt w/w) from 10.2% in 2020 and to improve 0.2ppt y/y to 13.2% in 2022 (unchanged w/w). The S&P 500's weekly reading of its forward P/E ticked up 0.1pt w/w to 21.1. That compares to 23.1 in early September, which was the highest level since July 2000 and up from a 77-month low of 14.0 in March 2020. The S&P 500 weekly price-to-sales ratio rose 0.03pt w/w to 2.79, matching its record high in mid-July. That compares to a 49-month low of 1.65 in March 2020.

**S&P 500 Sectors Forward Revenues and Earnings Recovery from Covid-19 Trough** (*link*): The S&P 500's forward revenues and earnings as well as its implied forward profit margin bottomed at cyclical lows on May 28, 2020 after 14 weeks of Covid-19-related declines. Forward revenues and earnings have risen 17.2% and 50.6%, respectively, since then to new record highs. The forward profit margin has risen 3.1ppts to a record high of 13.2%, exceeding its prior record high of 12.4% in late 2018. During the latest week, all 11 sectors posted gains to new highs in either their forward revenues, earnings, or profit margin. Here's how the 11 sectors rank by their changes in forward revenues and forward earnings since May 28, 2020: Energy (forward revenues up 27.2%, forward earnings up 1,553.6%), Materials (26.6, 90.0), Communication Services (24.1, 54.9), Information Technology (23.9, 41.0), Industrials (21.2, 65.9), S&P 500 (17.2, 50.6), Financials (14.0, 67.7), Health Care (13.8, 25.3), Consumer Discretionary (12.2, 87.7), Consumer Staples (9.9, 17.2), Real Estate (9.0, 24.9), and Utilities (0.4, 3.8).

## US Economic Indicators

**Housing Starts & Building Permits** (*link*): The US housing market is losing steam, as single-family starts and permits fall in July—the latter for the fourth successive month and the fifth time this year. Builder optimism has hit a wall, falling to a 13-month low this month, battling the headwinds from high construction costs and supply shortages. July housing starts sank 7.0%, the fourth decline this year, to 1.534mu (saar), after a two-month jump of 9.0%, though July's drop pushed starts down 7.6% ytd. Single-family starts contracted 4.5%

in July, and 15.5% ytd, to 1.111mu (saar), still a relatively high level, while volatile multi-family starts dropped 13.1% in July to 423,000 units (saar), though were up 22.3% ytd. Meanwhile, building permits—a good leading indicator of housing starts—increased 2.6% to 1.635mu (saar) last month, after a three-month slide of 9.2%, with permits down 7.0% ytd. Single-family permits sank for the fourth consecutive month, falling 1.7% m/m and 12.2% over the period to 1.048mu (saar)—down 17.4% from its cyclical high at the start of this year. Multi-family permits rebounded 11.2% in July to 587,000 units (saar), with these permits up 11.8% since the end of 2020, fluctuating in a very volatile flat trend. NAHB's August's Housing Market Index (HMI) shows builders' confidence continued to drift lower since reaching a record high in November, dropping from 90 to 75 over the period. All the components are trending lower, though remain at elevated levels near their November record highs: traffic of prospective homebuyers (to 60 from 77 in November), current sales (81 from 96), and future sales (81 from 89), though the latter has been fairly steady the past few months.

## Global Economic Indicators

**Eurozone CPI** (*link*): July's CPI headline rate matched its flash estimate, accelerating 2.2% y/y—the highest since October 2018—after slowing from a then-31-month high of 2.0% in May to 1.9% in June. Looking at the main components, once again energy (to 14.3% from 12.6% y/y) posted the biggest gain, recording its largest yearly gain since August 2008. Meanwhile, the yearly rate for food, alcohol & tobacco (to 1.6% from 0.5% y/y) was triple June's pace; the yearly increase in these prices had slowed steadily from 1.5% at the start of this year to 0.5% by May and held there in June. The services inflation rate ticked slightly higher in July, to 0.9% y/y, after slowing from 1.1% in May to 0.7% in June—which was the slowest since the end of 2020. The rate for non-energy industrial goods eased to 0.7% in July, after accelerating from 0.3% in March to 1.2% in June—the highest since the start of the year. Of the top four Eurozone economies, rates for Germany (3.1% y/y) and Spain (2.9) were above the Eurozone's headline rate of 2.2%, while rates for Italy (1.0) and France (1.5) were below.

---

Contact us by *email* or call 480-664-1333.

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-497-5306
Melissa Tagg, Director of Research Projects & Operations, 516-782-9967
Mali Quintana, Senior Economist, 480-664-1333

Jackie Doherty, Contributing Editor, 917-328-6848
Valerie de la Rue, Director of Institutional Sales, 516-277-2432
Mary Fanslau, Manager of Client Services, 480-664-1333
Sandy Cohan, Senior Editor, 570-228-9102