MORNING BRIEFING
May 5, 2022

Powell, Travel, Forward Earnings & Quantum Sensors

Check out the accompanying chart collection.

Executive Summary: Investors liked the middle-of-the-road approach Fed Chair Powell laid out after yesterday's FOMC meeting. We did too. … Travel-related industries are booming! Their Q1 earnings calls were brimming with optimism. Yet investors seem to have missed the memo: The share price indexes of most travel-related S&P 500 industries have plunged ytd ..: And it's not just a travel thing: Most industries are seeing disconnects between earnings prospects and share price performance. Someone's wrong: Either industry analysts are too optimistic in their estimates or investors too pessimistic about valuations. … Also: A developing technology with diverse potential uses: quantum sensors.

The Fed: Straight Down the Middle. Stock and bond market investors liked what they heard from Fed Chair Jerome Powell at his post-FOMC *press conference* yesterday. He drove right down the middle of the monetary tightening road, thus avoiding hitting the guard rails. He specified a likely speed limit of 50bps hikes in the federal funds rate at each of the next two FOMC meetings on June 14-15 and July 26-27. That would bring the rate's range up to 1.75%-2.00% by mid-summer. He downplayed the likelihood of a 75bps hike anytime soon.

Powell stressed that he and his colleagues are aiming for a soft landing. He even said that he believes that the Fed can bring inflation down, especially in the labor market, by weakening aggregate demand just enough to reduce all the excess job openings that are encouraging workers to quit at a record pace for better pay without pushing the unemployment rate up much. We wish him luck in this endeavor and think he might succeed.

Monday morning, we opined that there was too much pessimism in the stock market. On Tuesday, we observed that Joe Feshbach, our go-to trading pro, agreed with us and believed that Monday's reversal day set the stage for a solid rebound in stocks. On Wednesday, we also expressed the same opinion about too much pessimism in the bond market. Granted, yesterday's bullish action in stocks and bond were relief rallies, but we were relieved to see them unfold in response to Powell's down-the-middle presser.

We've previously described Powell as a "pragmatic pivoter." Currently, that means that he isn’t locking the Fed into an overly aggressive tightening policy stance. The financial markets like that, and so do we.

Consumer Discretionary: Travel Boom Arrives. After being cooped up for the better part of the last two years, Americans are packing their bags and hitting the road. Consumers are taking those long-postponed vacations, traveling for weddings, and visiting family and friends. Business travel appears to be picking up too, and trade shows have returned.

Travel-related companies reporting Q1 results this week have turned in strong revenue and earnings growth compared to last year. It may just be the start of a rebound that continues throughout this year. Q1 results were weighed down by the Covid resurgence in January (*Fig. 1* and *Fig. 2*). But cases since have fallen sharply, as have related hospitalizations and deaths.

The number of travelers passing through TSA checkpoints averaged 2.11 million per day in April, up from 1.48 million in January, 1.73 million in February, and 2.06 million in March. The number of travelers in April was up 52% y/y (*Fig. 3*).

Jackie traveled through Sin City’s airport recently and can attest to the hustle and bustle. The passengers arriving and departing from Las Vegas’ Harry Reid International Airport (the former McCarran International Airport) rose from 3.31 million in January and 3.34 million in February to 4.27 million in March. The number of March 2022 passengers is almost twice the 2.58 million passengers who passed through the airport in March 2021. I can report a similar experience getting through large crowds in Miami’s airport and scene.

Could the travel boom be imperiled by inflation? Certainly. The jump in the price of necessities could drain consumers’ pocketbooks so much that they postpone travel plans again. A new strain of Covid that causes a spike in hospitalizations could put a damper on the fun. We don’t even want to think about how the war in Ukraine could postpone US travel. That said, the Q1 earnings we perused looked good, and CEOs sounded optimistic on earnings conference calls. Here’s a look at some the highlights:

(1) *Cars getting rented.* Americans are packing up and hitting the open road. Avis reported a 77.3% jump in Q1 revenue to $2.4 billion and adjusted Q1 earnings per share of $9.99, up from a $0.46 loss the prior year and smashing Wall Street analysts’ forecast of $3.45 a share. Results benefitted from more cars being rented and at higher prices. The company also benefitted from the high price its used cars fetched when sold.

Avis' rebound is no surprise; its shares are up 37.6% ytd, and CEO Joe Ferraro was effusive about the current environment on the company's Tuesday *conference call*: "Consumer demand for travel is the highest we've ever seen. After two years of quarantine, video conference calls, and home improvement projects, consumers have now decided enthusiastically, to dedicate the best share of wallet to see the world and reconnect with loved ones."

Demand for car rentals was depressed during the Covid-wracked first six weeks of this year. But demand rebounded in March and continued to be strong throughout April. Today, the company has more reservations booked over 30 days in advance than it had in 2019, which implies that consumers are confident enough in their ability to travel that they're planning ahead.

"Every leading indicator that we typically follow—prepaid leisure bookings, corporate travel, cancellation rates, you name it—all of it points to the most robust demand environment we've ever seen. Most robust by a significant margin, I would say," said CFO Brian Choi on the conference call. Even international business bookings were positive in March compared to 2019 levels. The company didn't give earnings guidance for Q2 or full-year 2022.

Analysts are concerned this will be the peak year in earnings from Avis, in part because the company's results have benefitted from gains from the sale of its used cars. So while the consensus 2022 earnings estimate has been creeping up to $30.05 a share from $21.07 three months ago, analysts are calling for earnings per share of $18.53 in 2023.

(2) *Others optimistic too.* Airbnb reported that customers booked a record number of nights and experiences during Q1, exceeding pre-pandemic levels. An increase in nights booked and higher prices helped gross bookings grow 67% y/y to a record of $17.2 billion in Q1—more than 70% higher than pre-pandemic 2019 levels.

Demand continues to be strong: Airbnb had 30% more nights booked for summer by the end of April than it had during the same time in 2019. The company expects to post its first full-year profit this year. "The travel recovery that began in 2021 has accelerated into Q1 2022," the company's *press release* stated.

Marriott CEO Anthony Capuano also noted how strong the market was in the company's Q1 earnings *press release*: "During the first quarter, we saw the largest surge in global demand since the pandemic began in 2020." The company enjoyed revenue per available room (a.k.a. RevPar) gains in all of the company's regions except China. The worldwide average daily rate for March was 5% higher than the same month in 2019. Occupancy rates also improved as this year progressed, from 45% in January to 65% in March. The company expects “leisure travel to remain strong, business travel to accelerate, and cross border travel to gain momentum.”

(3) *Travel industry embraces tech.* Technology is being used throughout the travel industry to help companies cope with higher wages and unfilled job openings. In many cases, it also makes life easier for customers.

Avis QuickPass allows preferred customers to use their cell phone to pick out a vehicle, proceed directly to the car, and use a QR code to exit the lot via an automated Express Exit. With QuickPass, customers don’t need to wait in line at a counter and talk to an employee. The technology also allows customers to return the car and close the rental themselves. Avis aims to have the technology at most key airports by the summer travel season starts.

(4) *Industry & casinos data.* Outside of the airline industry, many travel-related stocks aren’t reflecting the optimism that executives are expressing about the upcoming travel season. Consider how the following travel-related S&P 500 price indexes have performed ytd through Tuesday’s close: Airlines (10.5%), Hotels, Resorts & Cruise Lines (-7.3), and Casinos & Gaming (-16.4) (*Fig. 4*, *Fig. 5*, and *Fig. 6*). They compare to the S&P 500 stock price index’s 12.4% decline.

Stocks of casino companies with exposure to Macao have been under pressure, as Covid cases in China have prompted the government to shut down certain cities and regions including Shanghai. Business was also shocked when China arrested a “junket” organizer who is accused of organizing illegal cross-border gambling. Las Vegas Sands, Wynn Resorts, and MGM Resorts International all are in the S&P 500 Casinos & Gaming industry, and all have exposure to Macao. Gross gaming revenue in Macau fell 68% y/y in April.

Caesars isn’t exposed to Macau, but its shares are down 27.7% ytd through Tuesday’s close because marketing expenses related to its online sports betting product have resulted in losses. But occupancy rates in the company’s Las Vegas hotels rose from 75% and 81% in January and February to 91% in March and just under 97% in April, a May 3 *article* in the *Las Vegas Review-Journal* reported.

The S&P 500 travel-related industries incurred losses last year, so their 2022 earnings growth can’t be calculated. However, here’s the revenue growth analysts are forecasting in 2022 for them and the S&P 500: Hotels, Resorts & Cruise Lines (60.0%), Airlines (53.4), Casinos & Gaming (20.3), and S&P 500 (10.1) (*Fig. 7*, *Fig. 8*, and *Fig. 9*).

Earnings: Someone's Wrong. Stock prices and forward earnings (which we calculate from industry analysts' earnings-per-share consensus estimates) have been moving in opposite directions this year: The S&P 500 stock price index has fallen 12.4% ytd through Tuesday's close, while forward earnings for the S&P 500 has increased 7.4% ytd.

This divergence isn't limited to the broad market benchmark; investors and analysts view the prospects for many of the S&P 500's sectors and industries differently as well. As the saying goes: Something's gotta give. Either the stock market is ripe for a bounce or analysts have a lot of estimates to cut. Let's take a look:

(1) *Positive revisions among sectors.* Just like the S&P 500, the stock price indexes of most of the S&P 500's sectors have fallen in value over the course of 2022 even as their forward earnings have risen.

Here's the derby for S&P 500 sectors' projected forward earnings growth and their stock price performance ytd through Tuesday's close: Energy (39.2%, 41.2%), Real Estate (11.8, -11.5), Information Technology (8.9, -17.5), S&P 500 (7.4, -12.4), Materials (7.0, -5.5) Consumer Discretionary (6.9, -20.2), Industrials (6.2, -9.3), Financials (5.9, -10.6), Consumer Staples (4.6, -0.8), Health Care (4.2, -8.0), Utilities (3.5, -1.2), and Communications Services (-1.9, -23.8).

(2) *Industries follow the same pattern.* We track more than 120 of the S&P 500 industries, and only 11 have had negative forward earnings revisions ytd (*Table*).

As you'd expect given the 36% ytd jump in the price of a barrel of oil, energy industries are among those enjoying the strongest upward earnings revisions this year. Likewise, the Ukraine war has pushed up agriculture and fertilizer prices, boosting earnings in related industries, which explains their improving earnings outlooks.

(3) *Top of the list.* Here are the 10 S&P 500 industries enjoying the strongest upward forward earnings revisions ytd: Hotel & Resort REITs (108.8%), Integrated Oil & Gas (47.1), Industrial REITs (39.2), Oil & Gas Exploration & Production (38.6), Oil & Gas Refining & Marketing (36.8), Fertilizers & Agricultural Chemicals (28.4), Research & Consulting Services (17.8), Agricultural Products (16.8), Trucking (16.1), and Homebuilding (15.9).

The Research & Consulting Services industry may be enjoying upward earnings revisions, but its stock price index has fallen 10.3% ytd through Tuesday's close. Likewise, the Trucking stock price index is down 19.4% ytd, and Homebuilding shares have fallen 29.9%.

(4) *More contradictions.* Regional Banks just missed making the top 10 list, but analysts' estimate revisions have boosted its forward earnings by 15.7% since the start of the year, even though investors have pushed down the industry's stock price index by 14.1% ytd.

Here are some other industries that have seen their forward earnings revised upward even as their stock price indexes underperformed the overall S&P 500 ytd: Advertising (12.7% ytd earnings revision, -2.0% ytd stock price performance), Semiconductors (12.4, -23.2), Automobile Manufacturers (11.5, -16.7), Distributors (11.3, -17.2), Specialty Stores (11.1, -12.9), Household Appliances (11.1, -18.8), Health Care Facilities (10.3, -14.2), Technology Hardware, Storage & Peripherals (10.0, -10.1), Building Products (9.5, -26.9), Electrical Components & Equipment (9.3, -18.2), Automotive Retail (9.1, -13.9), Internet & Direct Marketing Retail (9.0, -25.8), Life Sciences Tools & Services (9.0, -22.4), Investment Banking & Brokerage (8.9, -15.8), and Home Improvement Retail (8.8, -25.2).

Disruptive Technologies: Hyper-Sensitive Quantum Sensors. In the past, we've discussed the development of quantum computers and their use of quantum physics to perform calculations much faster than traditional computers (e.g., see the November 4, 2021 *Morning Briefing*). Scientists are also using quantum physics to develop quantum sensors to measure items with a precision that today's instruments cannot replicate.

Here's a quick look at what scientist hope quantum sensors of the future will be able to measure:

(1) *Better brain scans*. Scientists are using quantum sensors to more accurately measure the brain's electrical currents, an April 29 *article* in IEEE Spectrum reported. Cerca Magnetics, based in Nottingham, England, has designed an optically pumped magnetometer that "contains a laser that shins a beam through a cloud of rubidium atoms at a light detector. The beam can make the magnetic fields of the rubidium atoms all line up, rendering the cloud essentially transparent. Tiny magnetic fields, such as those from the brain activity, can disturb these atoms, making them capable of absorbing light, which the light detector can sense."

The new sensors work at room temperature and can be attached to a helmet, which gives patients mobility. They can also be placed closer to a person's head, which makes the signal more accurate.

(2) *Mapping the Earth.* A quantum sensor can map out what's underground by sensing the Earth's gravitational field. The Earth's field changes based on how much mass is in any specific area. This sensor could be used to discover underground structures—whether manmade, such as archeological sites, or natural like caves—and to monitor volcanic activity and groundwater flows, the IEEE article noted.

(3) *Detecting Covid.* A quantum sensor uses a defective diamond with a nitrogen atom instead of a carbon atom inside of it. The defect makes the material sensitive to magnetic fields. "The new technique involves coating nitrogen-vacancy-center diamonds roughly 25 nanometers wide with magnetic compounds that detach from the gems after they bond with the specific RNA sequence of the SARS-CoV-2 virus. When the diamonds are lit with green light they will emit a red glow," the IEEE article reported.

Other uses for quantum sensors include GPS that works underground and underwater, detects axions and other dark matter in space, and measures the heat within cells to determine how temperature influences cell division, gene expression, and other aspects of biology.

Calendars

US: Thurs: Productivity & Unit Labor Costs -5.4%/9.9%; Initial & Continuous Jobless Claims 182k/1.4m; Natural Gas Storage; OPEC Meeting. **Fri:** Payroll Employment Total, Private, and Manufacturing 394k/385k/35k; Average Hourly Earnings 0.4%m/m/5.5%y/y; Average Weekly Hours 34.7; Unemployment Rate 3.5%; Consumer Credit $25.0b; Baker-Hughes Rig Count; Williams; Waller. (Bloomberg estimates)

Global: Thurs: Germany Factory Orders -1.1%; France Industrial Production 0.2%; UK C-PMI & NM-PMI 57.6/58.3; BOE Interest Rate Decision & BOE QE Total 1.00%/842b; BOE Inflation Report; RBA Monetary Policy Statement; Lane; Beerman; Bailey. **Fri:** Germany Industrial Production -1.0%; Spain Industrial Production 2.7%; Italy Retail Sales; UK Construction PMI 58.0; Canada Employment Change 55k; Canada Unemployment & Participation Rates 5.2%/65.4%; Nagel. (Bloomberg estimates)

Strategy Indicators

Stock Market Sentiment Indicators (*link*):The Bull/Bear Ratio (BBR) continues to bounce around 1.00, moving back below this week. The BBR sank to 0.79 this week (the lowest since March 2020) after climbing from 0.96 to 1.04 last week. It's been hovering around 1.00 since late February. Bullish sentiment sank to 30.9% this week—the lowest since the 29.9% percentage at the end of February, which was the least bulls in two years. Meanwhile, bearish sentiment surged from 32.9% to 39.3% this week—the highest count since March 2020. The correction count fell for the second week, from 34.6% to 29.8%; it was as high as 40.0% in early February. The AAII Ratio fell for the third time in four weeks last week, plunging from 53.7% to 21.7% over the period—the lowest since March 2009, as bullish sentiment sank to 16.4% and bearish sentiment soared to 59.4%.

US Economic Indicators

ADP Employment (*link*): "In April, the labor market showed signs of slowing as the economy approaches full employment," said Nela Richardson, chief economist, ADP. "While hiring demand remains strong, labor supply shortages caused job gains to soften for both goods producers and service providers." Private payroll employment advanced 247,000 in April, the weakest since April 2020's pandemic-related drop, though reached another new record high at 129.4 million. These payrolls had averaged monthly gains of 530,700 the first three months of this year and 573,400 during 2021. ADP's employment report showed widespread gains, with service-providing companies adding 202,000 jobs and goods-producing 46,000. In April, leisure & hospitality (77,000) once again led gains among service-providing companies, followed by health care & social assistance (41,000), administrative & support services (28,000), professional & technical services (21,000), trade, transportation & utilities (15,000), financial activities (8,000), education (6,000), other services (6,000), and management of companies (1,000)—with information services (-2,000) showing a slight loss. Within goods-producing, manufacturing (25,000) was at the number one spot again in April, followed by construction (16,000)—though both gains were roughly half the average monthly gains recorded the first three months of this year. Meanwhile, natural resources and mining companies added 4,000 jobs—matching its Q1 average monthly increase. Here's a tally of industry performances relative to their pre-pandemic levels: trade transportation & utilities (+754,000), professional & technical services (+502,000), construction (+292,000), administrative & support services (+218,000), manufacturing (+66,000), health care & social assistance (+64,000), financial activities

(+57,000), education (-17,000), information services (-41,000), management of companies & enterprises (-47,000), natural resources & mining (-64,000), other services (-174,000), and leisure & hospitality (-459,000). Here's the same exercise by company size: medium (+410,000), large (+391,000), and small (+349,000), with small-business jobs falling 103,000 in April—its second decline in three months.

Merchandise Trade (*link*): The real merchandise trade deficit tumbled to a new record low of -$137.8 billion in March—widening from October's $96.5 billion gap. Both real exports (2.6%) and real imports (9.8) rose during the month, though imports accelerated at quadruple the pace of exports to a new record high—surpassing its previous record high by 21.5%! Trade was a major drag on real GDP last quarter, subtracting 3.1ppts, accounting for the unexpected decline in economic growth last quarter. Reaching new record highs in March were real imports of capital goods ex autos, consumer goods (nonfood) ex autos, and food, feeds & beverages. Real imports of industrial supplies & materials remain on a steep uptrend, jumping 9.7% in March and 24.2% from September 2020's recent low, while real imports of motor vehicles & parts climbed to a 14-month high. Meanwhile, there were no major moves in real exports with most moving sideways; the exception was real exports of consumer goods (nonfoods) ex autos, which is on a steep uptrend though has stalled recently.

US Non-Manufacturing PMIs(*link*): The service sector unexpectedly slowed in April, likely reflecting continued supply constraints exacerbated by new Covid lockdowns in China and the war in Ukraine. Meanwhile, prices accelerated at a record pace. The ISM's NM-PMI (to 57.1 from 58.3) eased in April though remained robust, but it was down dramatically from November's (68.4) record rate. The four measures that compose the index were a mixed bag. Production (65.1 from 63.4) accelerated last month, putting it above 60.0 for the 14th consecutive month albeit below the record rate of 75.7 recorded in October and November. Meanwhile, the new orders (54.6 from 60.1) gauge dropped back below 60.0, while the employment (49.5 from 54.0) measure slipped back below 50.0, into contractionary territory, after moving above in March; it has been fluctuating around the breakeven point of 50.0 the first four months of this year. The supplier deliveries' (65.1 from 63.4) measure continued to indicate slower deliveries, putting pressure on prices. April's prices-paid measure rose to an all-time high of 84.6 from 83.8 in March.

Global Economic Indicators

Eurozone Retail Sales (*link*): Eurozone retail sales in March fell 0.4%, more than the expected 0.1% shortfall, though remains in record territory—within 2.1% of November's record high. Sales of automotive fuels (-2.9%) and nonfood products excluding auto fuels (-1.2) dragged overall sales down, more than offsetting the rebound in sales of food, drinks & tobacco (0.8%), which reversed the declines posted the prior two months. Data are available for three of the Eurozone's four largest economies: Spain (-4.0%) recorded the largest decline in March, not only for the group but for the entire Eurozone. It was its third decline in four months, tumbling 8.8% over the period. It was also the weakest on a y/y basis, down 4.8%. Meanwhile, retail sales in France also contracted for the third time in four months, by 1.9% m/m and 1.6% over the period, though sales were up 1.8% y/y. Following suit, German retail sales also declined for the third time in four months, down 0.1% and 2.5% over the comparable periods, though sales were 2.7% below a year ago.

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