May 23, 2024

Morning Briefing

Transports,
Nvidia & ETs

Check out the accompanying chart collection.

Executive Summary: The economy is strong and the broad stock averages are hitting new records, but the Dow Jones Transportation index has been idling since 2021. What gives? Jackie explores what's been holding transport stocks back. What she found suggests that it might be time for the stocks to play catchup. … Also: Nvidia reported blowout Q1 earnings and announced a stock split and dividend increase to boot. Results imply the AI party will keep going. … And: With new regulations for its ports, California catalyzes the adoption of electric trucks; electric school buses in the state won't be far behind.

Industrials: Can Transports Get Back on Track? Amid all the bullishness surrounding the achievement of Dow 40K, there is one area of potential concern: transportation stocks. According to Dow Theory, strong economies bring increased shipping of goods, benefiting transportation companies and their stocks. But that hasn't been the case this year. While the Dow Jones Industrial Average has risen past successive milestones since 2021, the Dow Jones Transportation Average has essentially moved sideways (*Fig. 1*).

The same pattern holds true for the S&P 500, which has gained 11.6% ytd through Tuesday's close, while the S&P 500 Transportation stock price index has dipped 2.1% ytd. Most of the S&P 500 Transportation industry indexes are in negative territory so far this year with the exception of the airlines.

Here's the performance derby for the S&P 500 Transportation industries ytd through Tuesday's close: Passenger Airlines (17.1%), Transport Composite (-2.1), Cargo Ground Transportation (-2.2), Rail Transportation (-4.5), and Air Freight & Logistics (-5.2) (*Fig. 2*).

Some of the divergence between the S&P 500 and the S&P 500 Transports may be due to the increased importance of services and technology in the US economy. Companies don't need a truck to provide cloud computing or streaming services.

Another probable reason for transports' underperformance ytd is that some businesses haven't needed to restock their shelves because they've been working down excess inventory accumulated after the Covid buying boom. For example, retail inventories excluding motor vehicles and parts have slowly edged lower after shooting up 41.4% from June 2020 to August 2022 (*Fig. 3*).

But with inventories much leaner today and oil prices behaving, it may be time for transportation stocks to start working again. Here's a look at what's been moving the various transportation industries:

(1) *Trucking in neutral.* The amount of stuff being hauled around the country has been flattish for the past few years. The ATA Truck Tonnage Index, at 113.4 in March, is up from its recent low of 111.3 in January but still well below its 120.3 peak in 2019 (*Fig. 4*). Over the past six months, the cost to move freight by truck has been dropping; it was down 1.0% y/y in April (*Fig. 5*).

This hasn't been a conducive environment for truckers like J.B. Hunt Transportation Services. The trucking and logistics company's profit declined to $127.5 million in Q1, down from $197.8 million a year earlier, and Q1 revenue fell 9.9% to $2.9 billion. Likewise, Knight-Swift Transportation Holdings in April cut its Q1 and Q2 earnings estimates. J.B. Hunt's share price has fallen 20.2% ytd through Tuesday's close, and Knight-Swift's shares have dropped 19.4%. But analysts are expecting J.B. Hunt's earnings per share to improve from $6.97 in 2023 to $7.73 this year and $9.58 in 2025. Knight-Swift's earnings are also expected to climb, from $1.34 a share last year to $1.92 this year and $4.02 in 2025.

(2) *Off the rails.* The amount of goods traveling via rail has been declining for most of the time since 2021. This May railcar loadings fell to 466,000 units, basically flat versus a year ago (*Fig. 6*).

One bright spot is the recent pickup in container traffic flowing in and out of the West Coast ports. Railcar loadings at the West Coast ports have bounced 3.7% from their recent lows, though they remain far off their July 2021 highs. Likewise, the sum of the outbound and inbound containers have bounced 10.3% from their August 2023 lows, and they too are far from their summer 2021 highs (*Fig. 7*).

Earnings growth in the S&P 500 Rail Transportation industry is expected to speed up from the sluggish pace of 5.8% this year to 13.3% in 2025 (*Fig. 8*). Yet the industry's forward P/E of 18.3 is close to the middle of the range it has frequented over the past decade (*Fig. 9*).

(3) *Airlines flying high.* Consumers have returned to the skies in the years following Covid. The revenue passenger miles flown has almost completely recovered from its Covid-induced drop, as has the number of travelers passing through TSA checkpoints at airports (*Fig. 10* and *Fig. 11*).

The airlines also have benefitted from modest increases in industry capacity. Boeing's woes have severely limited the number of new planes it has delivered to airlines looking to retire older planes or to expand. Delta Air Lines' Q1 adjusted earnings per share almost doubled y/y—to 45 cents from 25 cents a year earlier—and bookings for the upcoming peak travel season are strong among both leisure and business travelers, according to Delta's earnings *press release*.

Since rebounding in 2021, the S&P 500 Passenger Airlines stock price index has been in a channel of lower highs and lower lows (*Fig. 12*). That said, the industry's net earnings estimate revisions have turned positive in recent months, and analysts are calling for the industry's earnings to rebound from this year's projected 1.4% decline to strong 20.2% growth in 2025 (*Fig. 13*).

(4) *Bad news priced in?* Air Freight & Logistics companies have had the toughest time of it this year, with the industry's stock price index down 5.2% ytd through Tuesday's close. Some of the pain is due to growing competition in the industry: FedEx and UPS have lost market share to Amazon, which ships its own products as well as the products sold by third-party retailers on its website.

Fortunately, from a contrarian perspective, there's a lot of bad news priced into the industry's shares. The shares of C.H. Robinson Worldwide rallied earlier this month despite the 14.0% y/y decline in the company's Q1 adjusted earnings per share of 86 cents. As it turns out, the results were 23 cents above Wall Street's consensus estimate and up 72% on a sequential-quarter basis. The company's shares popped 17% on the news, while the S&P 500 inched up 0.4% that day, a May 2 *Barron's* *article* reported.

Net earnings estimates revisions have yet to turn positive in the Air Freight & Logistics industry, but analysts are optimistic that earnings will do so this year, rising 3.5%, and gaining a more impressive 15.0% in 2025 (*Fig. 14*). Yet the industry's forward P/E, at 15.2, is low relative to where it has been over the past two decades (*Fig. 15*).

Information Technology: Nvidia Delivers a Beat. It has been a while since a company's earnings release made stock investors hold their collective breath. But that's exactly what happened prior to Nvidia's earnings release yesterday. A lot was riding on the AI bellwether, and the company delivered.

Nvidia reported Q1 revenue that soared to $26.0 billion, up 262% from the $7.2 billion it generated in the same quarter last year. Results beat Wall Street's consensus expectation of $24.6 billion in revenue. The chip company posted net income of $14.9 billion, compared to the $2.0 billion it earned a year ago and above Wall Street's forecast of $13.1 billion. And finally, the company's adjusted earnings per share came in at $6.12, 461.5% above the $1.09 a share reported last year and well past analysts' estimates of $5.60.

Were that not enough good news, Nvidia announced a 10-for-1 stock split and increased its quarterly cash dividend to 10 cents per share, up from 4 cents per share, on a pre-split basis. The company also forecast sales of $28.0 billion, plus or minus 2%, in Q2, above analysts' consensus forecast of $26.6 billion, a CNBC *article* reported.

In aftermarket trading shortly after the release, Nvidia shares gained 5.1%, rising $48.56 to a new high of $998.06.

Clearly, Nvidia's AI chips have retained their dominance, but many other tech companies would like to chip away some of Nvidia's success. Advanced Micro Devices has an AI chip, the MI300, that Microsoft offers to its cloud computing customers as an alternative to Nvidia's H100 chips. Intel launched Gaudi 3, an AI chip that it claims is faster than Nvidia's H100 and will be competitive with Blackwell, an excellent April 19 *Barron's* *article* on the competitive chip landscape reported. And Qualcomm has its Cloud AI 100 offering.

Nvidia also faces competition from chips created by its customers, Amazon, Google, Meta Platforms, and Microsoft. And there are also a handful of startups gunning to become the next AI chip giants. But so far, Nvidia remains the company to beat.

Disruptive Technologies: Electrifying Trucks. Electric trucks (ETs) are hitting the road in California. The Golden State passed a rule requiring that trucks purchased after the start of this year must be zero-emission vehicles if they want to service the state's ports. The rule also phases out the use of older diesel trucks used at the ports until they are all banned by 2035.

Many truckers bought diesel trucks last year in anticipation of the rule change. But now some large companies, including Amazon and Pepsi, have started to buy large ETs to operate in California. It's a slow transition, with only 246 of the state's 218,490 registered drayage trucks currently propelled by an electric battery.

ETs are more expensive to purchase than diesel trucks, and they may reduce the driver's productivity—in one case cutting the number of deliveries a trucker can make in a day from six to two because of the time needed to charge the vehicle, a December 29 *WSJ* *editorial* reported.

Here's more on the electrification of trucks—as well as school buses and vans—in the state:

(1) *Amazon's ETs.* Amazon is adding 50 fully electric Volvo Class 8 semis to its trucking fleet in California. These ETs, which can travel 275 miles on a charge, will transport cargo containers and customer package loads. Amazon has also purchased Ford and Rivan electric vans to deliver packages the "last mile" to homes and businesses in California.

(2) *Pepsi's ETs.* Pepsi announced that 50 Class 8 Tesla semi trucks will operate out of its manufacturing and distribution facility in Fresno, California. The company also plans to use 75 Ford E-Transit electric vans throughout the state as part of its net-zero-emissions-by-2040 goal.

(3) *Startups' ETs.* California's new rules provide new opportunities for startups like Hight Logistics. Hight has 45 diesel trucks and plans to have 20 ETs by summer, a March 18 *Fast Company* *article* reported. The ETs will charge at Hight's facility near the Port of Los Angeles and make 160-mile roundtrips between the port and warehouses.

(4) *Schools' EBs.* The Oakland Unified School District was the first to go fully electric with its 74 electric buses (EBs). The school district is partnering with Zum, a student transportation company, to test the benefits of selling the power stored in the buses' batteries back to the California utility. Zum's "goal is to add 10,000 bidirectional EV school buses across the US with 300 gigawatt hours of energy available to power grids each year," a May 15 CNBC *article* reported. The San Francisco and Los Angeles school districts are expected to use EBs as well.

Buses are well suited to serve as a virtual power plant because their ample downtime provides opportunities to charge them at times when power is cheap and sell electricity back to the grid when it's in demand and expensive. This could help schools pay for the EBs, which are two to three times more expensive than as traditional buses.

Calendars

US: Thurs: New Home Sales 674k; Kansas City Fed Manufacturing Index; Initial Claims 221k; M-PMI & NM-PMI Flash Estimates 50.1/51.5; Natural Gas Storage; Bostic. **Fri:** University of Michigan Consumer Sentiment Index Total, Current Conditions, and Expectations 67.4/68.8/66.5; University of Michigan One-Year & Five Year Inflation Rates 3.5%/3.1%; Atlante Fed GDPNow 3.6%; Headline & Core Durable Goods Orders -0.5%/0.1%; Baker-Hughes Rig Count. (FXStreet estimates)

Global: Thurs: Eurozone, Germany, and France M-PMI Flash Estimates 46.2/43.2/45.8; Eurozone, Germany, and France NM-PMI Flash Estimates 53.6/53.5/51.8; UK M-PMI & NM-PMI Flash Estimates 49.5/54.7; UK Gfk Consumer Confidence -18; Eurogroup Meetings; Pill. **Fri:** Germany GDP 0.2%q/q/-0.2%y/y; France Business Survey 100; UK Retail Sales -0.6%; Canada Headline & Core Retail Sales -0.1%/-0.2%; Eurogroup Meetings; Schnabel; Nagel; Mauderer. (FXStreet estimates)

Strategy Indicators

Stock Market Sentiment Indicators (*link*): The *Bull-Bear Ratio* rose for the fourth week to 3.45 this week after falling from 4.43 seven weeks ago—which was the highest reading since February 5, 2018—to 2.15 four weeks ago. *Bullish* sentiment rose for the fourth week to 59.4% this week after retreating the previous three weeks from 62.5% to 46.2%, which was the lowest percentage since late October. Meanwhile, *bearish* sentiment slipped for the fourth week to 17.2% this week after climbing to 21.5% four weeks ago; it was at 14.1% in early April—which was the fewest bears since 12.6% in late January 2018. The *correction count* fell for the third week to 23.4% this week after climbing the prior four weeks from 23.4% to 33.3%, which was the highest since early October 2023. Turning to the *AAII Sentiment Survey* (as of May 16), pessimism fell during latest reporting week, while optimism was unchanged and neutral sentiment increased. The *percentage expecting stocks to fall over the next six months* slipped 0.6ppts to 23.3%, with pessimism below its historical average of 31.0% for the second time in five weeks. The *percentage expecting stock prices to rise over the next six months* was unchanged at 40.9%, remaining above its historical average of 37.5% for the 27th time in the past 28 weeks. The *percentage expecting stock prices will stay essentially unchanged over the next six months* edged up 0.5ppts to 35.9%, with neutral sentiment above its historical average of 31.5% for the fourth time in nine weeks.

S&P 500 Earnings, Revenues, Valuation & Margins (*link*): The S&P 500's forward profit margin remained steady w/w at an 18-month high of 13.1% during the May 16 week. That's up from a 24-month low of 12.3% during the March 30, 2023 week and just 0.3pt below its record high of 13.4% achieved intermittently in 2022 from March to June. It's now 2.8pts above its seven-year low of 10.3% during April 2020. Forward revenues rose less than 0.1% w/w to a hair below its record high during the May 2 week. Forward earnings remained steady w/w at a record high. It had hit that mark during the September 21 week for the first time since the June 16, 2022 week. Revenues and earnings had been steadily making new highs from the beginning of March 2021 to June 2022; prior to that, they peaked just before Covid-19 in February 2020. The consensus expectations for forward revenues growth remained steady w/w at an 18-month high of 5.3%. It has gained 3.0pts from its 33-month low of 2.3% during the February 23, 2023 week. That's down from a record high of 9.6% growth at the end of May 2021 and compares to 0.2% forward revenues growth during April 2020, which was the lowest reading since June 2009. The forward earnings growth forecast remained steady w/w at a 30-month high of 12.2%. It's now 8.9pts above its 31-month low of 3.3% during the February 16, 2023 week. That's down from its 23.9% reading at the end of April 2021, which was at its highest since June 2010 and up substantially from its record low of -5.6% at the end of April 2020. Analysts expect revenues to rise 4.7% in 2024 (up 0.1pt w/w) and 5.6% in 2025 (unchanged w/w) compared to a revenues gain of 2.2% in 2023. They expect an earnings gain of 10.4% in 2024 (unchanged w/w) and a 14.1% rise in 2025 (up 0.1pt w/w) compared to an earnings gain of 2.4% in 2023. Analysts expect the profit margin to rise 0.7ppt y/y to 12.6% in 2024 (unchanged w/w), compared to 11.9% in 2023, and to rise 1.0ppt y/y to 13.6% in 2025 (unchanged w/w). The S&P 500's weekly reading of its forward P/E rose 0.5pt w/w to a seven-week high of 20.8, but remains below its 26-month high of 21.1 at the end of March. That's up from a 30-month low of 15.3 in October of 2022. It also compares to 23.1 in early September 2020, which was the highest level since July 2000, and to a 77-month low of 14.0 in March 2020. The S&P 500 weekly price-to-sales ratio rose 0.06pt w/w to a 28-month high of 2.72. That's up from a six-month low of 2.22 during the October 26 week and compares to a 31-month low of 1.98 in October 2022. That also compares to a record high of 2.88 at the end of 2021 and a 49-month low of 1.65 in March 2020.

S&P 500 Sectors Earnings, Revenues, Valuation & Margins (*link*): Looking at the 11 S&P 500 sectors during the May 16 week, seven had forward revenues that rose w/w, and six had forward earnings that moved higher. This led to a gain in forward profit margins too, as five sectors moved higher w/w on that measure. Real Estate is the only sector with forward revenues at a record high this week as these three sectors edged down from their records a week earlier: Health Care, Industrials, and Information Technology. Among the remaining seven sectors, only three have forward revenues more than 5.0% below their post-pandemic highs: Energy, Financials, and Materials. These four are less than 1.5% from their recent record highs: Communication Services, Consumer Discretionary, Consumer Staples, and Utilities. When adjusted for the incoming transfer of five former Tech sector firms in March 2023, Financials' forward revenues would be at a record high. Two sectors have record-high forward earnings this week: Communication Services and Consumer Discretionary. Consumer Staples, Industrials, Information Technology, and Utilities were in that camp in very recent weeks, and Financials would be too when adjusted for GICS changes in March 2023. Among the remaining four sectors, two still have forward earnings down more than 20.0% from their post-pandemic highs: Energy and Materials. Looking at the forward profit margin, nearly all of the sectors are showing signs of recovering from their early 2023 forward profit margin lows. Communication Services, Consumer Discretionary, and Information Technology are the only sectors with their forward profit margin at a record high this week. In recent weeks, Industrials was in that camp as well. Energy's forward margin is improving now from its 23-month low of 10.4% in February, while those of Consumer Staples and Health Care remain at or close to their record lows. The annual profit margin is expected to fall y/y in 2024 for Energy, Materials, and Real Estate and improve for the other eight sectors. Here's how the S&P 500 and its 11 sectors rank based on their current forward profit margin forecasts along with their record highs: Information Technology (26.7%, a new record high this week), Financials (19.0, down from its 19.8 record high in August 2021), Communication Services (17.7, down from its 17.8 record high a week earlier), Real Estate (17.0, down from its 19.2 record high in 2016), Utilities (13.8, up 0.1pt w/w and from its 14.8 record high in April 2021), S&P 500 (13.1, unchanged at an 89-week high, but down from its record high of 13.4 achieved intermittently in 2022 from March to June), Materials (11.0, unchanged w/w at a 30-week high, but down from its 13.6 record high in June 2022), Energy (10.9, unchanged w/w and down from its 12.8 record high in November 2022), Industrials (10.7, unchanged w/w and down from its 10.8 record high in early April), Consumer Discretionary (9.1, unchanged w/w at a record high), Health Care (8.6, unchanged w/w at 0.1pt above its record low at the end of April and down from its 11.5 record high in February 2022), and Consumer Staples (6.9, unchanged w/w and down from its 7.7 record high in June 2020).

US Economic Indicators

Existing Home Sales (*link*): "Home sales changed little overall, but the upper-end market is experiencing a sizable gain due to more supply coming onto the market," noted Lawrence

Yun, NAR's chief economist. *Existing home* sales in April unexpectedly fell for the second month as mortgage rates remain high, falling by 1.9% m/m and 5.5% over the two-month period to 4.14mu (saar). They had increased three of the prior four months by an impressive 13.8% over the period to 4.38mu (saar), up from its recent low of 3.85mu. April sales are 1.9% below a year ago. *Single-family* sales dropped 2.1% in April and 5.8% over the two months ending April to 3.74mu (saar), after soaring three of the previous four months by 15.4% from 3.44mu to 3.97mu; April sales were 1.3% below last April's pace. *Multi-family* sales were unchanged in April at 400,000 units (saar), though were 7.0% below a year ago. *Regionally*, existing home sales in April fell in all four regions, with the Northeast (-4.0%) posting the biggest decline, followed by the West (-2.6), South (-1.6), and Midwest (-1.0%). Total *housing inventory* at the end of April was 1.21 million units, up 9.0% from March and 16.3% from last April's 1.04 million units—with unsold inventory at 3.5 months' supply at the current sales pace, up from 3.2 months in March and 3.0 months in March 2023. The *median price* of an existing home for all housing types in April was $407,600, up 5.7% from April 2023—the tenth successive y/y gain and the highest price ever for the month of April. All four regions registered price gains in April.

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

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Eric Wallerstein, Chief Markets Strategist, 201-661-3575
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-241-6502
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