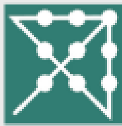
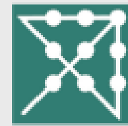
 Yardeni Research 

July 11, 2024

# Morning Briefing

## Homebuilders, Regulations & Microcapacitors

*Check out the accompanying chart collection.*

**Executive Summary:** With today's unusual housing market dynamics undercutting the affordability of new homes, homebuilders are offering buyers sales incentives. So far, they're working to companies' advantage, Jackie reports: Lennar's May-quarter revenue and earnings both jumped around 9% y/y. We continue to watch rising inventories. … A recent Supreme Court ruling effectively transfers power from the government's regulatory agencies to the judiciary system. That could mean softer regulations on Corporate America going forward and lots of litigation. … And in our Disruptive Technologies segment: A super powerful microcapacitor being developed could help meet the growing demand for mini energy storage units in microdevices like Internet-of-Things sensors and AI processors.

**Homebuilders: Costly Sales.** With interest rates on home mortgages bouncing around 7.00%, it's no wonder that homebuilders are offering incentives to attract buyers and make home purchases more affordable (*Fig. 1*). In the June 20 *Morning Briefing*, we noted that Lennar executives told analysts on the company's earnings conference call that incentives on home deliveries in its quarter ended May 31 were 9.4% of revenue. Lennar disclosed additional details about its incentives in its *10Q*, as *highlighted* by the sharp-eyed folks at Wolf Street.

Unfortunately, most other homebuilders aren't disclosing such details about their sales incentives, though they do acknowledge offering incentives. So, under the heading of "no good deed goes unpunished," let's share some of the incentives information Lennar provided in its latest earnings report and put it into context with some housing market stats:

(1) *Incentives helping spring sales.* In the three months ended May 31, the average sales incentive per home Lennar delivered was $44,200, up from $41,000 in the same period last year. Regionally, incentives ranged from a low of $37,400 in Central US to a high of $47,900 in the East. However, the company's "Other" segment, which includes its Urban division and some California investments, had a much higher average sales incentive of

$73,400, down from $101,800 a year ago.

Sales incentives as a percentage of revenue in the May quarter averaged 9.4%, ranging from a low of 8.4% in Central US to a high of 15.9% in Texas. February-quarter incentives were even more elevated, at 10.9% of revenue. Incentives have climbed sharply from 1.5% in the May 2022 quarter.

(2) *Company color.* Lennar explained its use of incentives in its 10Q as a response to unusual housing market dynamics: "[C]onsumers are generally employed and are confident that they will remain employed and that their compensation is likely to rise. This is most often the foundation of a strong housing market, but the chronic supply shortage, the impact of interest rates on affordability and persistent and stubborn inflation have moderated housing market strength. In response, we and other homebuilders have worked out sales incentives to meet the purchasers at the intersection of need and affordability to enable purchasers to buy homes. With our ready access to capital, we have been able to adjust and capture demand by using incentives to reduce the affordability constraint."

Despite the incentives, Lennar reported May-quarter revenue that rose 9.0% to $8.8 billion and net income that jumped 9.4% to $960.6 million. But as we previously reported, its forecast for the current quarter came in below analysts' expectations. Lennar's stock price has fallen 4.4% ytd through Tuesday's close. That's only a touch worse than the S&P Homebuilding stock price index's 3.6% ytd decline (*Fig. 2*).

(3) *Impact on inflation?* The Census Bureau's report on new residential sales uses data on contract prices, which don't reflect the cost of mortgage-rate buydowns or other incentives, according to the folks at Wolf. If that's the case, home prices as reflected in the Census data may be overstated.

New homes sold in May had a median price of $417,400, down slightly from April's $417,900 and down a bit more sharply from the median price a year ago of $421,200, according to Census *data*. Conversely, the average price of a new home continues to rise. It was $520,000 in May, higher than the average new home sold in May 2023 at $495,800 (*Fig. 3*). The discrepancy reflects a preponderance of homes sold at lower price points.

(4) *Supply building.* Beyond new home prices, we continue to watch the growing number of homes available for sale. The months' supply of new homes on the market rose to 9.3 months in May. That figure reflects a calculation of how long the number of new homes on the market would take to sell at the current sales pace (*Fig. 4* and *Fig. 5*).

The supply of existing homes for sale is rising as well, as listings continue to hit the market and sales have slowed. Active listings of homes for sale jumped 36.7% y/y in June to 840,000, according to a July 9 Wolf Street *report* citing Realtor.com data. The number of homes on the market is just shy of 2020 levels at this point in the year. Listings are roughly between the lowest levels of 2021 and the pre-pandemic highs of 2017.

In some areas, the surge of homes on the market in June is even more dramatic. The largest increases in listings occurred in the Tampa area (up 93.1% y/y), followed by Orlando (81.5%) and Denver (77.9%), according to data from Realtor.com. The data include new homes when they are on the Multiple Listing Service.

**Strategy: Federal Agencies' Power Challenged.** A recent Supreme Court ruling has dramatically diluted the power of federal agencies and increased the power of the judiciary. The decision also has the potential to affect a wide swath of Corporate America—basically any company that follows federal regulations and policies set by the DOE, the DOL, the FCC, the FTC, OSHA, the SEC, or any of the entire alphabet soup of federal agencies in the US government.

The Supreme Court ruled on June 28 in *Loper Bright Enterprises v. Raimondo* that the interpretation of administrative law is the sole and exclusive function of the judiciary. The ruling was a major policy reversal. Since the 1984 Supreme Court's decision in *Chevron USA Inc. v. Natural Resources Defense Council,* the judiciary had largely deferred to federal agencies when it came to interpreting the law.

"The implications are far reaching and profound," *wrote* our friend James Lucier at Capital Alpha Partners in reaction to the ruling on June 28. "The ruling would affect almost anything the federal government does—from health care, to labor law, financial services regulation, tech and telecom to tax and tariffs." And by inference, it will affect the corporations that are governed by those regulations.

While it's early days, we can only presume that federal agencies may respond to the ruling by taking a softer approach when setting new policies to avoid being challenged in court. It may prevent agencies from reaching beyond their directives laid out in federal legislation, which they've been accused of doing in the past.

We'd also expect a slew of lawsuits by corporations aiming to eliminate or amend federal agencies' regulations and by nonprofit organizations looking to strengthen regulations they

believe are too weak. The Supreme Court ruling could also increase jurisdictional conflicts and compliance headaches for companies with operations in multiple states if a regulation is successfully challenged in one state's court and invalidated in another's, noted a June 28 *report* by Jackson Lewis, a firm specializing in labor and employment law.

The Supreme Court clearly indicated that the new policy would be forward looking and not apply to any cases that were decided based on the Chevron principal in the past. That said, the *Loper Bright* decision appears to be a giant gift to the Bar Association.

Here's a brief look at how the new Supreme Court decision might affect existing and pending regulations:

(1) *DOE & energy efficiency.* One of the first regulatory rules Capital Alpha's Lucier believes will be eliminated is the Petroleum-Equivalent Fuel Economy Calculation, or PEFEC. Simply put, manufacturers of electric vehicles get credits they can trade. Critics from both the conservative and liberal camps argue that the manufacturers get more credits than they deserve, so it's likely they will challenge the rule in court.

(2) *FCC & net neutrality.* The Biden administration's efforts to revive net neutrality may be D.O.A. after the *Loper Bright* decision. Net neutrality was first enacted under the Obama administration, only to be eliminated under President Trump. To revive net neutrality, the FCC under President Biden reclassified Internet providers as public utilities; that provoked lawsuits trying to prevent the reclassification, a June 29 *WSJ* *article* reported.

(3) *FTC & noncompete contracts.* After the Supreme Court ruling, a Federal Trade Commission (FTC) ban on noncompete contracts is on shaky ground, the *WSJ* article added. The agency's rule prevents employers from using noncompete agreements to stop workers from joining rival companies. Expected to go into effect in September, the ruling has faced opposition in the past, and it's reasonable to expect objectors to bring the case to the courts.

(4) *EPA & clean air.* The Environmental Protection Agency (EPA) introduced new rules, Clean Power Plan 2.0, to reduce pollution from coal-powered plants that will likely be challenged in the courts. The outcome will be watched closely by those looking to build new plants to meet the energy demands of the new data center capacity required for the proliferation of artificial intelligence.

Under the EPA regulations, coal plants that are expected to operate beyond 2039 will have

to reduce carbon emissions by 90% by 2032; the sooner the plant is expected to close, the lower the emissions reduction required. The rules also affect plants that use natural gas, with carbon emissions reductions levered to the frequency of plant operation, according to a May 3 *primer* by the World Resources Institute. (For example, plants operating more than 40% of the time would face carbon emissions reductions equivalent to 90% carbon capture and sequestration by 2032.)

Lucier also expects the Clean Air Act Section 177 waiver that allows California to ban the sale of gasoline-powered cars and require all new cars to be zero-emission vehicles to be challenged successfully in the courts.

(5) *SEC & its authority.* The Securities and Exchange Commission (SEC) has put forward a number of controversial rules in recent years that may face scrutiny. Rules requiring climate disclosures, private funds, and digital assets may now be challenged, according to a online *post* by law firm Foley & Lardner.

**Disruptive Technologies: Energizing Microcapacitors.** A team of researchers from the MIT Lincoln Laboratory, UC Berkeley, and the Lawrence Berkeley National Laboratory has created a microcapacitor that has nine times higher energy density and 170 times higher power density than those on the market today, a May 6 Berkeley Lab *press release* reported. The team’s work may lead to electronic devices that are even smaller and more efficient than today’s.

Let’s take a look at the advancement:

(1) *Capacitor vs battery.* Capacitors typically hold a small amount of energy that’s tapped when brief surges of power are needed. In an electrical circuit, electrons travel from one metal plate in the capacitor through a wire to another metal plate in the capacitor. Energy is stored in the electric field created between the capacitor's two metal plates. A battery uses electrodes and an electrolyte to store chemical energy that is converted to electrical energy.

Capacitors can charge and discharge more rapidly than batteries but historically have had less energy density. Capacitors also last longer and charge faster than batteries. A microcapacitor can be recharged billions of times, while a microbattery can be charged only 1,000 times. And a microcapacitor can be charged 100 million times faster than a battery.

(2) *How they did it.* The scientists used engineered thin films of hafnium oxide and zirconium oxide separated by amorphous aluminum oxide. The extremely thin layers were

placed on the silicon surface of a U-shaped DRAM (dynamic random access memory) semiconductor chip.

(3) *What it means.* It's hoped that microprocessors will extend the life of implanted medical devices, power small robots, or energize Internet-of-Things devices. And in the future, low-power silicon chips may not need external power. They might also be more energy efficient because the energy doesn't have far to travel.

"These high-performance microcapacitors could help meet the growing demand for efficient, miniaturized energy storage in microdevices such as Internet-of-Things sensors, edge computing systems, and artificial intelligence processors. The researchers are now working on scaling up the technology and integrating it into full-size microchips, as well as pushing the fundamental materials science forward," the Berkeley Lab press release stated.

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## Calendars

**US: Thurs:** Headline & Core CPI 3.1%/3.4$ y/y; Jobless Claims 236k; Federal Budget Balance; Natural Gas Storage; IEA Monthly Report; Bostic. **Fri:** Headline & Core PPI 0.1%m/m/2.2%yy & 0.2%m/m/2.5%y/y; University of Michigan Consumer Sentiment 67.0; Baker-Hughe Rig Count; WASDE Report. (FXStreet estimates)

**Global: Thurs:** Germany CPI 0.1%m/m/2.2%y/y; UK GDP 0.2%m/m; UK Headline & Manufacturing Industrial Production 0.3%/0.3%; ECOFIN Meetings; Eurogroup Meetings. **Fri:** Germany WPI 0.2%; France CPI 0.1%m/m/2.1%y/y; Spain CPI 0.3%m/m/3.5%y/y; Japan Industrial Production 2.8%; Eurogroup Meetings. (FXStreet estimates)

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## Strategy Indicators

**Stock Market Sentiment Indicators** (*link*): The *Bull-Bear Ratio* slipped to 3.50 this week, after climbing to an 11-week of 3.73 last week. It was at 4.43 14 weeks ago—which was the highest reading since February 5, 2018. *Bullish sentiment* fell to 62.7% this week after climbing the prior four weeks by 5.5ppts (to 63.1% from 57.6%) and was just above the March peak count of 62.5%—which was the most bulls since 2021. Meanwhile, *bearish sentiment* rebounded to 17.9% this week after falling from 18.5% to 16.9% last week, which was the fewest bears since just 14.1% in late March 2024 (which also saw the last high for

the bulls). The *correction count* edged down to 19.4% this week from 20.0% in each of the prior two weeks. it was at 33.3% 10 weeks ago—which was the highest since early October 2023. Turning to the *AAII Sentiment Survey* (as of June 27), both optimism and pessimism among individual investors about the short-term outlook for stocks rose during the latest reporting week, while neutral sentiment fell. *Bearish sentiment* jumped 5.8ppt o 28.3%—remaining below its historical average of 31.0% for the seventh time in 11 weeks, while *bullish sentiment* barely budged, ticking up 0.1ppt to 44.5%, remaining above its historical average of 37.5% for the 33rd time in 34 weeks. Neutral sentiment increased 6.0ppts to 27.2%, above its historical average of 31.5% for eighth successive week.

**S&P 500 Earnings, Revenues, Valuation & Margins** (*link*): The S&P 500's forward profit margin rose 0.1pt w/w to a 24-month high of 13.3% during the July 4 week. That's up from a 24-month low of 12.3% during the March 30, 2023 week and just 0.1pt below its record high of 13.4% achieved intermittently in 2022 from March to June. It's now 3.0pts above its seven-year low of 10.3% during April 2020. Forward revenues rose 0.5% w/w to a new record high. Forward earnings surged 1.0% w/w to a record high too. It had hit that mark during the September 21, 2023 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 rose 0.2pts w/w to a 21-month high of 5.6%. It has gained 3.3pts 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 rose 0.3pts w/w to a 33-month high of 13.2%. It's now 9.9pts 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 5.9% in 2025 (up 0.1pt w/w) compared to a revenues gain of 2.2% in 2023. They expect an earnings gain of 10.5% in 2024 (down 0.1pt w/w) and a 14.7% rise in 2025 (up 0.2pts w/w) compared to an earnings gain of 2.5% 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 (down 0.1pt w/w). The S&P 500's weekly reading of its forward P/E remained steady w/w at a 30-month high of 21.2. 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 0.01pt w/w to a 30-month high of 2.81. That's up from a six-month low of 2.22 during the October 26, 2023 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 July 4 week, all 11 had forward revenues and forward earnings that moved higher. This led to rising forward profit margins w/w for nine of the 11 sectors. These six sectors had forward revenues at a record or post-pandemic high this week: Communication Services, Consumer Discretionary, Consumer Staples, Health Care, Industrials, and Information Technology. Financials' forward revenues would be at a record high too when adjusted for the incoming transfer of five former Tech sector firms in March 2023. Two sectors remain less than 0.7% below their recent post-pandemic highs: Real Estate and Utilities. The two remaining sectors have forward revenues more than 5.0% below their post-pandemic highs: Energy and Materials. Five sectors have record-high forward earnings this week: Communication Services, Consumer Discretionary, Industrials, Information Technology and Utilities. Financials would be too if adjusted for GICS changes in March 2023. Just two sectors still have forward earnings down more than 19.8% from their post-pandemic highs: Energy and Materials. Among the remaining three sectors, Consumer Staples is 0.1% from its recent record high, while Health Care and Real Estate are 6.4% and 3.6% below their highs. Looking at the forward profit margin, nearly all of the sectors are showing signs of recovering from their early 2023 forward profit margin lows. Information Technology is the only sector with a forward profit margin at a record high this week. In recent weeks, Communication Services, Consumer Discretionary, and Industrials were in that camp as well. Energy's forward margin is up to 10.8% now from its 23-month low of 10.4% in February, while those of Consumer Staples and Health Care remain at or slightly above their record lows. The annual profit margin is expected to fall y/y in 2024 for Energy, Materials, and Real Estate and to 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 (27.2%, up 0.1pt w/w to a new record high), Financials (19.2, up 0.1pt w/w and down from its 19.8 record high in August 2021), Communication Services (17.8, record high this week), Real Estate (17.1, up 0.1pt w/w and down from its 19.2 record high in 2016), Utilities (14.0, up 0.1pt w/w and down from its 14.8 record high in April 2021), S&P 500 (13.3, a 24-month high and just 0.1pt below its record high of 13.4 achieved intermittently in 2022 from March to June), Materials (11.2, up 0.1pt to a 16-month high and down from its 13.6 record high in June 2022), Energy (10.8, down 0.1pt w/w from its recent six-month high and down from its 12.8 record high in November 2022), Industrials (10.8, up 0.1pt w/w to match its record high from September 2023), Consumer Discretionary (9.1, a record high this week), Health Care (8.7, up 0.2pts from its record low at the end of April and down from its 11.5 record high in February 2022), and

Consumer Staples (6.9, down from its 7.7 record high in June 2020).

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