



## MORNING BRIEFING

May 11, 2017

### On the Road Again

See the [collection](#) of the individual charts linked below.

(1) Leaving home. (2) Time for fun. (3) Cruising for dollars. (4) Spending on lasting memories on the high seas. (5) More Asians with wanderlust. (6) The hotels are occupied. (7) Having magical days at the theme parks. (8) More CEOs talking about wage pressures. (9) Labor shortages. (10) Peak plastic? (11) India going from cash to mobile pay. (12) Selfie Pay: Look into my eye.

**Industry Focus: Hospitality Sweet.** With the Great Recession all but a faded memory and summer rapidly approaching, staycations are out and vacations are in! Almost 80% of individuals contacted plan to take at least one weekend trip in 2017 and nearly two-thirds of them plan to travel more than 150 miles from home, according to a 12/21 [survey](#) by Enterprise Holdings.

Fun-related industries have had some of the best performances so far this year. S&P 500 Casinos & Gaming is the best-performing industry, up 42.7% ytd, while S&P 500 Hotels, Resorts & Cruise Lines has risen 25.2%, and S&P 500 Restaurants is up 14.9%. This implies that consumers are spending, just not at the mall. Strong Q1 earnings results out of some of the largest names in the travel industry drove home the strength in the market. Let's look at the results out of Royal Caribbean, Marriott International, and Disney:

(1) *Smooth sailing.* Royal Caribbean Cruises beat Q1 earnings expectations, and management boosted the company's 2017 forecast, saying its ships are booking up faster than last year, yields came in better than expected, and costs were lower than expected.

CEO Richard Fain spoke a bit about how consumer demand had evolved during the company's Q1 [conference call](#). A few years ago, if you asked consumers what they wanted, they might have said a flat-screen TV or a better car. Now people prefer to spend time with family, doing things that will make lasting memories. "I do think that [this is] somewhat of a culture shift and I think we're benefitting from that," said Fain. This trend has increased demand for vacations that include multiple generations of families, and it has boosted demand for excursions on cruises.

Royal Caribbean is also benefitting from the wanderlust of the rapidly expanding Chinese middle class, which will be bigger than the entire population of the US or Europe within the next few years. Right now, business in China is challenged by that country's directive to cruise operators to stop selling trips that stop at South Korea. Tensions between the two countries rose after South Korea deployed a US missile defense system. Royal Caribbean [redirected](#) its ships to Japan, and any Q1 weakness in China was offset by strength in Europe and elsewhere.

The cruise operator said adjusted net income rose 73.1% y/y to \$214.7 million and EPS rose to 99 cents, up from 57 cents and nine cents higher than the company's guidance. The company lifted its full-year EPS estimate by 10 cents to \$7.00-\$7.20. It also announced a new \$500 million stock repurchase program.

Shares of Royal Caribbean and other cruise operators also have benefitted from rumors that China's

HNA Group might be interested in buying a major cruise line, according to a 5/1 [report](#) in Cruise Industry News. HNA, which has a cruise brand in China, purchased a 16.8% stake in Dufry, which runs duty-free shops around the world, and purchased a stake in Rio's airport last month.

Investors will need to watch how expanding capacity in the industry from newly built ships being delivered in the next few years is absorbed. As of December, 26 new ocean and river cruise ships were on order, followed by another 17 ordered for 2018 and 22 for 2019, according to the [State of the Cruise Industry](#) published by the Cruise Lines International Association. But for the moment anyway, investors should enjoy these halcyon days.

(2) *No room at the inn.* Marriott also [reported](#) stronger-than-expected Q1 earnings and increased future earnings guidance. The company credited its strong performance to more customers staying at its hotels, higher room rates, more hotel rooms in its system, and a late Easter.

Marriott's worldwide revenue per available room (RevPAR) in constant dollars rose 3.1% in Q1. The gain is impressive given that the company added more than 17,000 rooms in the quarter. It also increased its development pipeline by nearly 10,000 rooms. Q1 adjusted net income was \$395 million, a 36% increase assuming the September merger with Starwood occurred at the start of 2015 and excluding merger costs. Adjusted EPS jumped 38% to \$1.01, above the company's 87-91 cent guidance.

Marriott increased its expectations for 2017 RevPAR in the US, Europe, and Asia. However, it left expectations unchanged in the Middle East, where geopolitical unrest, low oil prices, and lower government spending continued to depress results. All in all, the company increased its 2017 worldwide RevPAR estimate by 50bps from its previous guidance to 1%-3%. Company shares rose 6.4% in the wake of the report.

Similar to the cruise industry, the future of the hotel industry rides on whether demand will keep up with new supply. There are 560,199 US hotel rooms in 4,621 projects under construction or in planning stages as of December, a 19.4% y/y increase in the number of rooms, according to a 1/16 [article](#) in HotelNewsResource.com.

(3) *Happiest place on earth.* Weakness at ESPN may have captured the headlines about Disney's fiscal Q2 earnings, but the strength at the company's theme parks saved the day. Revenue at the parks increased 9% to \$4.3 billion, and operating income jumped 20% to \$750 million. Results were helped by a 4% increase in attendance at the US parks and the opening of Shanghai Disney last year, the company [reported](#).

(4) *By the numbers.* Hotels, Resorts & Cruise Lines has been one of the S&P 500's top-performing industries, gaining 25.2% ytd through Tuesday's close ([Fig. 1](#)). The industry has outperformed each of the S&P 500's sectors, including Technology.

Here is how the sectors have fared ytd: Tech (17.1%), Consumer Discretionary (11.6), Health Care (9.6), S&P 500 (7.1), Industrials (6.6), Consumer Staples (6.2), Materials (5.7), Utilities (5.3), Real Estate (2.0), Financials (1.7), Telecom (-10.6), and Energy (-10.8) ([Table](#)).

The Hotels, Resorts, & Cruise Lines industry (CCL, MAR, RCL, and WYN) is expected to grow revenue 9.6% over the next 12 months and earnings 13.7% ([Fig. 2](#)). The industry's forward P/E of 17.1 is modestly below a recent peak of 22.2 in 2013 ([Fig. 3](#)).

The S&P 500 Casinos & Gaming industry, which counts Wynn Resorts (WYNN) as its sole member,

has enjoyed a revival thanks to booming business in Las Vegas and Macau. Macau's gross gambling revenue was up 18% in March, continuing a recovery that began last August. The Casinos & Gaming industry is expected to grow revenue 17.4% over the next 12 months and earnings 30.2% ([Fig. 4](#)). Its forward P/E, at 24.5, is less than its anticipated earnings growth over the same period ([Fig. 5](#)).

**Earnings: Pay Hikes.** One of the interesting nuggets shared by Marriott's CEO Arne Sorenson in the company's Q1 conference call was about the labor market. "Construction costs have moved higher and we've seen some project delays in North America due to shortages of skilled subcontractors," he said.

His comments were the latest anecdotal evidence that the labor market is getting tighter. Modest wage increases have started to show up in the official data. Hourly compensation in nonfarm businesses rose 3.9% y/y during Q1 ([Fig. 6](#)). Here are some additional anecdotes:

(1) *Competitive landscape.* Rising wages were mentioned by executives at more than 24 large companies as part of discussions about Q1 earnings results. The companies were scattered among industries as diverse as financials, services, and manufacturers, the 5/4 [WSJ reported](#).

State Street raised base salaries by an average of 3%, effective in April, following years of small increases. "We thought it was important given the competitive landscape and the importance of keeping our top talent," said State Street's CFO Michael Bell.

LyondellBasell Industries is seeing wages escalate as it is expanding an ethylene plant, and other companies have plans for similar projects. Robert Half International saw rising pay for the temp workers it supplies to clients. And Avery Dennison reported that productivity gains and sales growth narrowly outpaced higher employee wages.

(2) *Contractors scrambling.* As business picks up, contractors in the commercial real estate industry are seeing shortages of electricians, carpenters, and other subcontractor workers, the 5/6 [WSJ reported](#). Commercial construction employment has almost returned to levels last seen in 2008, just as the country's unemployment rate has fallen to 4.4% and business has picked up.

The trade association Associated Builders and Contractors Inc. estimates that the industry needs 500,000 more workers. The group estimates an additional 600,000 workers will be needed if President Trump pushes through a \$1 trillion infrastructure building and improvement package. As a result of the tight labor market, construction labor costs are rising by an average of 4% to 5% annually, the article reported.

(3) *Fewer H-1Bs.* Indian information technology outsourcing companies have applied for fewer H-1B visas this year due to uncertainty about what the Trump administration will do to the program, according to a 5/7 [WSJ article](#). Conversely, the number of applications by US tech companies has remained steady, the article stated. Overall, applications fell 16% this year.

Yet to be seen is whether the Indian outsourcers will opt to hire Americans, outsource the work to India, or replace US workers with technology. Infosys announced plans to open a center in Indiana in August that will create 2,000 jobs for Americans by 2021. However, "Artificial intelligence, cloud technologies and bots now allow computers to do many of the routine tasks traditionally done by low-level IT workers such as monitoring servers, resetting passwords, fixing basic computer problems and providing tech support."

**Payments Technology: Peak Plastic?** Changes are coming fast to the world of payments. In India, use of mobile payments is growing faster than all other forms of payment and Mastercard is introducing

iris scans to improve security when making a mobile payment. Let's take a look:

(1) *Leapfrogging*. Mobile payments are taking off in India, propelled by the government's decision to replace its largest bank notes with newly designed ones. The government was aiming to curb corruption, counterfeiting, and boost its tax base.

"The value of mobile money transactions has more than doubled since the nullification of 86% of India's cash in circulation in November, while those made with credit and debit cards has fallen, and check purchases have barely budged. Mobile payments still make up only a small percentage of overall transactions, but their surging popularity is being noticed," the 4/29 *WSJ* [reported](#). The article speculated that India might move right from cash to mobile payments, skipping credit cards, just as some emerging markets skipped using phone land lines and went directly to adopting mobile phones.

Mobile payments are attractive to India's mom-and-pop businesses, which don't want to spend money on phone lines and swiping machines needed for credit cards. The expense seems unnecessary given that fewer than 5% of Indians have a credit card. Paytm is the leading mobile wallet in India, with 218 million wallets, and it counts Alibaba Group Holding as one of its investors.

Everyone wants into the market that grew 104% from October through February. Facebook, Amazon, Samsung, and Apple are either looking at the market or have launched a product. Meanwhile, the credit card companies have developed a system that allows users to scan a code with their phones to make a payment.

(2) *Hello, James Bond*. Mastercard CEO Ajay Banga discussed plans to use iris scans to improve mobile transaction security during the company's Q1 [conference call](#). The technology is the latest advancement in Mastercard Identity Check, better known as "Selfie Pay," an app rolled out last year. It initially used facial recognition and fingerprints to confirm identities. Now iris scanning technology will also be available later this year.

To use facial recognition, consumers simply take a selfie of themselves. The phone won't confuse the user and a picture of the user because it requires the user to blink. Likewise, the app can tell the difference between a human and a video because it can sense depth.

The advent of iris scans brings reality awfully close to fiction. Recall that the character Tom Cruise played in the movie "Minority Report" used eye transplants to trick identifying eye scanners. You know it's only a matter of time.

## CALENDARS

**US. Thurs:** Jobless Claims 244k, PPI-FD Total, Core, and Core Ex Trade Services 0.2%/0.2%/0.2%, Weekly Consumer Comfort Index, EIA Natural Gas Report, Dudley. **Fri:** Retail Sales Total, Ex Autos, Ex Autos & Gas, and Control Group 0.6%/0.5%/0.4%/0.4%, Business Inventories 0.1%, Consumer Sentiment Index 97.3, Headline & Core CPI 2.3%/2.0% y/y, Baker-Hughes Rig Count, Evans, Harker. (Bloomberg estimates)

**Global. Thurs:** UK Headline & Manufacturing Industrial Production 1.9%/3.0% y/y, BOE Rate Decision & Asset Target 0.25%/435b, BOE Inflation Report, ECB Publishes Economic Bulletin, G7 Finance Ministers Meet. **Fri:** Eurozone Industrial Production 0.3%/m/m/2.3%/y/y, Germany GDP 0.6%/q/q/1.7%/y/y(wda), Germany CPI 0.0%/m/m/2.0%/y/y. (DailyFX estimates)

## STRATEGY INDICATORS

**Stock Market Sentiment Indicators** ([link](#)): The Investors Intelligence Bull/Bear Ratio (BBR) climbed for the third week this week from 2.84 to a 3.39 over the period, a ten-week high. Bullish sentiment rebounded 6.8ppts over the three-week period to 58.7%, moving back toward its 63.1% reading ten weeks ago—which was the most bulls since 1987! Bearish sentiment slipped from 17.9% to 17.3% this week, dropping to the bottom of the narrow band (17.3% to 18.3%) it has fluctuated in since the first week of March. Meanwhile, the correction count climbed to 24.0% after falling to a nine-week low of 23.6% last week. The AAll Bull Ratio advanced for the second week last week from 39.9% to 56.0%. Over the two-week period, bullish sentiment rose from 25.7% to 38.1%, while bearish sentiment fell from 38.7% to 30.0%.

**S&P 500 Earnings Season Monitor** ([link](#)): With 89% of the S&P 500 companies finished reporting Q1-2017 results, their revenue and earnings surprise metrics are stronger than at the comparable point of the Q4 season, but Apple's results have impacted the y/y earnings growth results. Of the 447 companies in the S&P 500 that have reported, 76% exceeded industry analysts' earnings estimates by an average of 6.7%; they have averaged a y/y earnings gain of 8.0%, down from 10.8% before Apple reported. Ex-Apple, S&P 500 Q1 earnings growth improves 3.7ppts to 11.7%, and Tech's growth rate rises 15.5ppts to 10.2% from -5.3%. At the same point in Q4-2016, a lower percentage of companies (68%) in the S&P 500 had beaten consensus earnings estimates by a smaller 3.7% and ex-Apple earnings were up a lower 10.4% y/y. On the revenue side, 64% beat sales estimates so far, coming in 0.8% above forecast and 8.6% higher than a year earlier. During Q4, a lower 50% had revenues above forecast, which exceeded estimates by a smaller 0.1% and rose a lower 4.0% y/y. Q1 earnings results are higher for 62% of companies versus a greater 69% at the same point in Q4, but revenues are higher for 79% versus a lower 71%. The S&P 500's 6.7% earnings beat is the highest in eight quarters, and the 0.8% revenue surprise is the best in nine quarters. The percentage of companies with a positive earnings surprise (76%) is the highest since Q1-2010, and those with a positive revenue surprise (64%) is the highest since Q2-2014. Although the percentage of companies with positive y/y earnings growth weakened q/q to 62% in Q1, the percentage of companies with positive y/y revenue growth (79%) was the highest since Q3-2011. The results to date are very encouraging and bode well for future estimate revision activity. However, y/y growth is likely to slow in the coming quarters as comparisons become less easy.

**S&P 500 Earnings, Revenues & Valuation** ([link](#)): S&P 500 consensus forward revenues and earnings rose to record highs last week and at their fastest pace since late 2016. The forward profit margin forecast rose to 10.9% from 10.8%, marking its first record high since September 2015 and up from a 24-month low of 10.4% in March 2016. Forward revenue growth for the S&P 500 edged down w/w to 5.4% from 5.5%. That compares to 5.8% in late January, which was the highest since May 2012 and up from a seven-month low of 2.7% in late February 2016. Forward earnings growth improved to a 14-week high of 11.2% from 11.0%, but is down from 11.7% in early January; that was the highest since October 2011 and compares to an 11-month low of 4.8% in February 2016. S&P 500 forward revenues and forward earnings growth are enjoying a tailwind now due to easy y/y comparisons for Energy and improving prospects for Financials, but currency translation is likely to be a slight drag. However, Energy's contribution to forward growth peaked at the start of 2017. Looking at last week's results for the S&P 500 ex-Energy, the forward growth rates for revenues (4.4%) and earnings (8.8%) are lower. The ex-Energy forward profit margin improved to 11.5% from 11.4%, matching its record high of 11.5% in August 2007. Valuation fell to 17.6 from a four-week high of 17.7, which compares to a 13-year high of 18.0 in early March and a 15-month low of 14.9 in January 2016. Ex-Energy valuation fell to 17.2 from a six-week high of 17.3, and is down from a 13-year high of 17.6 in early March.

**S&P 500 Sectors Earnings, Revenues & Valuation** ([link](#)): Consensus forward revenue forecasts rose last week for 9/11 sectors, and forward earnings rose for 10/11. Telecom had both measures decline

w/w and Energy had forward revenues fall. Forward revenues and earnings are at or around record highs for 5/11 sectors: Consumer Discretionary, Consumer Staples, Health Care, Industrials, and Tech. Energy's forward revenues and earnings are stalling recently near 15-month highs. Forward P/S and P/E ratios fell broadly w/w, but Tech had both measures rise. Financials' P/E is up from 12.0 before the election to 13.5, but that's down from a post-election high of 14.6 in early March. Health Care's P/E of 15.7 and P/S of 1.66 are down from early March's 19-month highs of 16.1 and 1.70, respectively, and remain well below their early 2015 highs of 17.9 and 1.88, respectively. With Energy's forward revenues and earnings improving, its valuation is beginning to come back to Earth; its P/S ratio of 1.31 compares to a record high of 1.56 in May 2016, and its P/E of 25.9 is down from a record high of 57.5 then. Higher y/y margins occurred for only 7/11 sectors in 2016, and margins are expected to improve in 2017 for all but Real Estate and Utilities. However, Real Estate's forecasted margin should improve as the year progresses when gains on property sales are included in the forecasts. Here's how the 11 sectors rank based on their current 2017 forecasts: Information Technology (to 19.7% in 2017 from 19.2% in 2016), Real Estate (16.3, 25.2), Financials (15.8, 14.4), Telecom (11.3, 11.2), Utilities (10.9, 11.4), S&P 500 (10.6, 10.1), Health Care (10.4, 10.3), Materials (10.0, 9.4), Industrials (9.1, 8.8), Consumer Discretionary (7.3, 7.2), Consumer Staples (6.8, 6.5), and Energy (4.3, 1.1).

## US ECONOMIC INDICATORS

**Import Prices** ([link](#)): Import prices in April advanced 4.1% y/y, easing for the second month from February's 4.7%—which was the biggest 12-month gain since February 2012. It had bottomed at -11.6% in September 2015. Petroleum prices advanced 43.8% in the 12 months through April, down from February's seven-year high of 74.3%. Nonpetroleum product prices accelerated 1.5% y/y—turning positive in December (0.3% y/y) for the first time since November 2014. Total import prices rose for the fifth month, by 0.5% m/m and 1.9% over the period, with nonpetroleum prices up 0.4% m/m and 0.8% ytd. Moves in petroleum prices have been much less volatile the past several months, climbing 1.6% in April after a 0.4% loss and a 0.9% gain the previous two months.

---

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 & Webmaster, 570-775-6823

Copyright (c) Yardeni Research, Inc. Please read complete [copyright and hedge clause](#).