

## Current Economic Situation Report

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*This research project was conducted as part of Polygence — an online research academy that introduces secondary school students to cutting-edge research under the guidance of leading academics. Learn more at [www.polygence.org](http://www.polygence.org).*

## 1. Executive Summary

We are currently in the middle of the COVID-19 pandemic. But whenever there is a bad situation, there will always be excellent opportunities. One good potential investment is the cruise industry: it currently offers a very low price per share for companies like Norwegian, Royal Caribbean, and Carnival. Even though there are other industries that are very attractive to invest in, the cruise industry is the most attractive.

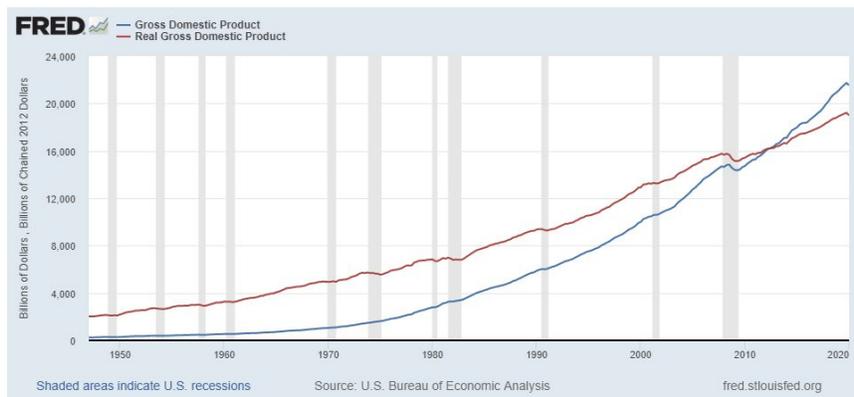
This financial crisis will probably follow the footsteps of the 2008 financial crisis, where the stock market plummeted, recovered, and plummeted again. They are similar because of the stock market that we see right now. The news has not gotten any better recently: high unemployment rate, the chance of a second wave of Coronavirus, and many more uncertainties. These could potentially lead to big sell-offs in the stock market.

We are currently on the rebound because the S&P 500 has just recently experienced the best 50 trading days ever, and many stocks have not only recovered but also reached a record high. With the stock market so optimistic about the future, this is a sign that suggests that we are on the rebound. Even so, the market will be unlikely to grow more. The market will probably trade sideways for a few months and then plummet another time in the fall, where the virus could potentially enter the “second wave” again.

## 2. The Real Economy

### 1. Overall Activity

Real GDP per capita, which is GDP adjusted for inflation and population growth, is a good indicator of how the economy is performing. It represents the total value of all finished goods and services produced within an economy each year. This is a useful indicator because it can inform us about how the economy is doing overall.



For an average person, a rising GDP indicates a higher overall income for the population; therefore, it also translates into higher living standards. Thus, we can gather some clues about how the economy will go in the near future. We have seen a sharp drop in both the GDP and the Real GDP. Almost all the industries dropped economically to some degree, some were severely impacted, and some only took some “bruises.”

The retail sales value has also decreased dramatically. From the graph below, we can see that the overall value of sales has decreased, and due to this decrease, many brands that are familiar to us have either filed for bankruptcy or, at least, having a hard time surviving this pandemic.



## 2. The Labor Market

The unemployment rate in 2020 so far has already skyrocketed from one of the all-time lows of 3% to nearly 15% as of April. The higher the unemployment rate, the fewer money people will spend, just like what happened during the great depression. This led to a sharp decrease in consumer spending. These astonishing numbers also reflect in the real world, with substantial pressure on the government to bring more people back to work. However, there are still too many concerns around getting back to work, for example, health care, proper equipment, and many other required items to keep the workers safe. Therefore, the unemployment rate will likely stay at a high number for quite some time.



### 3. Consumer Spending

There is a decrease in the amount of personal disposable income in 2020 due to the dramatic increase in the unemployment rate, as you can see down below in the graph.



Personal disposable income represents the spare money from their income that a person can spend after taxes. A decrease in personal disposable income essentially means that people have less spare money to spend, and most companies will also see a reduction in demand for their products. Though the extent to which a company is affected will depend on what the company sells. For example, products like hand sanitizer, masks, and gloves could be very popular products because they are in need during this pandemic. However, tickets from cruises will not sell well at all because there is nearly no demand at all for those at least until next year. Therefore, most companies will see a decrease in demand and profit, they will lay off

or fire workers to maintain the company itself. This will exacerbate the situation of this crisis because it led itself back to the increased unemployment rate.

Another reason that consumer spending continues to decrease is that the mandated closures of retail and leisure related establishments. Due to their closure, the situation has been compounded because people who want to spend their money cannot spend on these related activities. Therefore, having a higher average disposable income is essential not only to the spenders but also to the economy.

### 3. The Financial Economy

#### 1. Inflation



The government has taken many steps to prevent the economy from completely shutting down during the COVID-19 pandemic/economic crisis. First, the Federal Reserve adopted aggressive monetary policy measures by lowering interest rates and lending money to the private sector. Taxing would be unwise right now because most people are already struggling to pay their bills. Thus, the government is unlikely to raise taxes. Instead, it has actually increased spending by adopting a stimulus measure to send checks to most American citizens.

These stimulus checks can achieve many purposes that would otherwise be nearly impossible to achieve. First, they can alleviate the pressure of the unemployed. Since the unemployment rate has already hit almost 15%, that means that around 33 million people have lost their job due to Coronavirus. These stimulus checks will help people who are currently

struggling. Second, they can be used to stimulate the economy. When qualifying people (that is, adults with American citizenship making no more than \$75,000) receive their \$1,200 stimulus check, they will be able to purchase more. That, in turn, will hopefully lead to a positive cycle for the economy to grow. With this tremendous amount of money injected into the economy, inflation is inevitable; but it is not a bad thing since the alternative may be a complete shutdown of the economy.

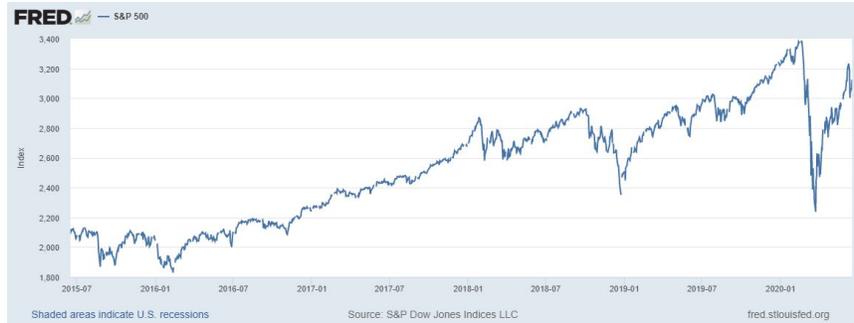
Although the numbers and the inflation seem terrible, it actually will not affect people living in the United States, or people mainly spending the US dollar. There are more people than you think that want the US dollar right now. For example, big corporations internationally, which are not based in the US, would want to transfer their liquidity into the dollar because the dollar is the most recognizable currency in the world; therefore, it is not likely that it will experience massive inflation. We all know that when everyone wants one thing, the price of this thing increases. Thus, despite all the money printed by the Fed, the dollar will not actually inflate by a ton, all because of the large number of people and corporations that want to transfer capital here.

## 2. Credit Markets

The Fed Funds Rate is currently at 0.05%. That means that the interest rates are very low. A low-interest rate attracts more people and companies to take their money out of the banks; since they know that leaving them in the bank, their money will not even be able to beat the rate of inflation. Therefore, they are losing money. Once people realize this, they will take their money out of the banks and are more likely to spend them. Thus, this is one of the ways that the Fed could stimulate the economy.

## 3. Equity Markets

The equity market is basically the stock market. The stock market is very volatile currently, and what we can tell from the numbers is that it has plummeted since January. Until today (July 4th, 2020), it had a significant rebound at a tremendous rate (shown in the graph below, this is the S&P 500).



The tech-sector of the market, measured by NASDAQ, has already completely recovered. The Dow Jones Industrial Average, by contrast, is still around 5,000 points below its all-time high. Another crucial view that the equity markets provide us is that some industries are not recovering as well or maybe not at all; therefore, this is one of the advantages that we can use in order to make our choices for investments, which I will discuss below.

#### 4. Investment Proposal

##### 1. Market Analysis

Since the market is not performing very well and also may have another drop in the future, it is a good time to buy into companies that are undervalued. The types of companies that we need to look for are the companies that have a high chance for surviving another potential upcoming crash. A large amount of liquidity, for example, would make a company more likely to survive. It will be ideal if these companies also owe a relatively small amount of debt so that they would not be threatened to pay their debt, which could make one company bankrupt.

The cruise industry is a great industry to invest in because it plays a critical role in the economy and the traveling industry. Americans love cruises. While the airlines and hotels are receiving canceled bookings and returned tickets, the cruise companies are only receiving delays on their customers' trips. That means that most Americans still believe that the situation will get better soon. This also shows that the cruise line companies still have a high demand instead of no demand, like the airlines and hotels. Another reason that the cruise industry is essential to the United States because it employs so many people. According to [cruising.org](http://cruising.org), the cruise industry provided the United States 420,000 jobs last year in 2019.

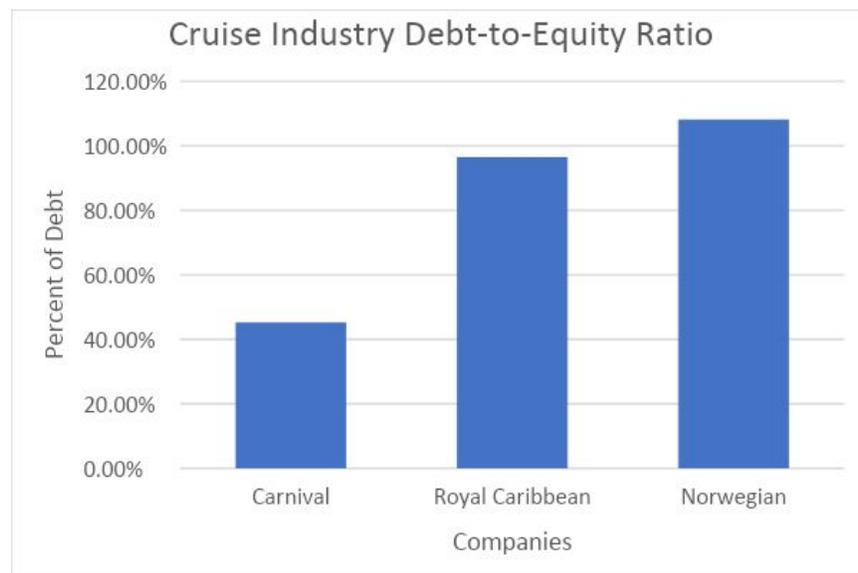
Even though the cruise industry seems very stable, there is the chance that it will fall to an even lower price or even bankrupt, and the investments could become essentially worthless. Due to the coronavirus outbreak, people may be more hesitant to take cruises than they were in the pre-pandemic world. Therefore, investing in right now is a good decision but do not plan to exit out of the market early on; if you invest, you are playing a long-term ball game.

## 2. Company Analysis

There are three big companies in the cruise industry: Royal Caribbean, Norwegian, and Carnival. Out of the three companies, Carnival is the biggest one with the most brands and ships in its fleet.

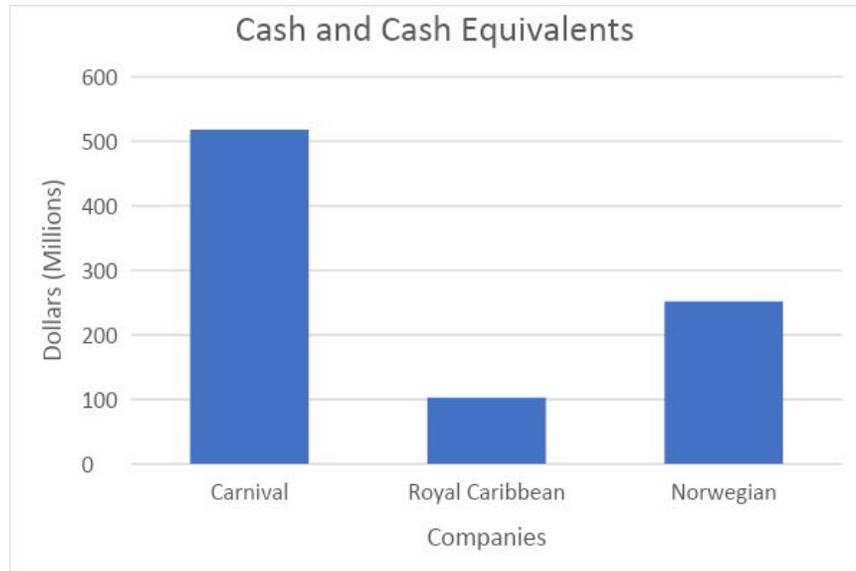
### Debt

Carnival is the company with the least amount of debt out of these three, with a debt-to-equity ratio of 45.3% to 54.7%. That may seem high, but both Norwegian and Royal Caribbean have debt-to-equity ratios over 100%. They are, therefore, a greater risk of failure than is Carnival during the pandemic.



### Liquidity

The data down below are from the 10-k of these companies, which are the annual financial reports from companies stating how well they are doing financially. Carnival has around \$500 million in cash, which is much higher than its competitors. Norwegian has the second most amount of cash out of the three companies, with around \$252 million. Royal Caribbean has the least amount of cash, with only around \$103 million.



### Value

From my calculations (total valuation subtracted by the total amount of debt that it holds), Carnival should be worth around \$28 billion. But the stock market is currently valuing it at only \$9.5 billion. Therefore, it is an excellent potential investment because the market is too pessimistic about Carnival’s ability to withstand the current crisis and recover when the COVID crisis ends.

### Overall:

I believe that Carnival is a much better buy than the other two companies. Carnival has less debt and more liquidity; both are critical numbers when there is a financial crisis and will help them survive. Even though I do believe that there is a great possibility that the cruise industry will diminish in size overall in the next two years, but I still believe that there is a way to a comeback. Once there is a reliable vaccine, fewer people will be fearful about the situation, and therefore, more people will get back on cruises.

### 3. Exit Plan

#### *Considerations While Holding Carnival*

The first thing to do is to identify the trend. Make sure that you know if the market is going up or down in general. If the market is continuously going up, cruise companies are likely to follow the trend; therefore, there is no need to do anything except for holding on.

Another thing to make sure that you are always clear about is the current price and your initial purchasing price. Sometimes, there are steep drops in the process of a long-term bull-market; thus, some new investors will panic when they see the situation and the tremendous amount of money that they lost in a few days. Since this occurred to me many times during the COVID-19 pandemic, there is one key takeaway as an investor, buy low and sell high without panic. This may seem very cliché, not only to investors but almost everyone with some basic knowledge, but I bet that there are only a few people that can actually follow and utilize this rule correctly.

One thing that you should always do as an investor is to keep up with the big news. Keeping up with the news can help one make better decisions with more recent data and events happening. Once there is news that could potentially affect the companies that you have invested in, you can decrease the number of shares that you are holding, or sell them all at a reasonable price. (this depends on how the news will affect the company: if it is something like another virus outbreak, you might want to consider selling a majority of your shares or even all. If it is a cruise ship accident, you might want to consider selling a small portion of your shares, although it depends on how bad it is and how it will tarnish the company's reputation.)

#### *Considerations on When to Sell Carnival*

After investing in this company, exiting out of it will also be hard to time, but do not worry, I have a good idea. Let us imagine that the price per share reached \$44 per share, and your purchase price is \$22 per share. At the time that it reached \$44 per share, only exit out of the market with half of the shares that you have and leave the other half and keep them. This method allows for many advantages that are, otherwise, impossible to achieve.

First, the first half of the shares that exited out of the market at \$44 per share guaranteed no loss. For example, you bought 100 shares of CCL at \$22 per share (total: \$2,200), and you sold 50 shares at \$44 per share (total: \$2,200), you bought yourself a risk-free investment. Even if Carnival goes bankrupt and not able to pay you your money back from your investment, you still have a loss of \$0.

The other advantage that this method has is that it allows for maximum profit but also achieving it with zero risks. Maximum profit can be made with zero risks because the 50 shares that you have not exited out of the market yet can be used for long term investing. Let us imagine that the stock price of Carnival went up to \$88 per share (although it is not very realistic in the near future). If the stock price is \$88 per share than the 50 shares that you

purchased at \$22 per share will become \$3,300 on top of the \$2,200 that you have already made.

**Please note that this method will only be a good way to exit if the current price of the shares is already double the amount of your initial average purchase price.**

## 5. Conclusion

I believe that the economy is currently in a bad situation, and the stock market simply does not make any sense. But I still believe that there will be another big crash ahead in the next few months.

There are many good investments that an investor can make during this time, and I chose the cruise industry. I believe that this industry will recover in the next few years but perhaps not as quickly as we would expect, and the industry will likely contract. Some cruise lines will go bankrupt.

Carnival has the best chance out of the three biggest cruise companies to survive the financial crisis. Therefore, I believe that there is a chance that both Royal Caribbean and Norwegian Cruises will go bankrupt, and Carnival will be the only one left in the industry. If this happens, Carnival will have a monopoly in the cruise industry, which could result in a much higher share price. It is, therefore, a good investment to buy CCL at \$11 and reassess whether to hold it weekly. Reassess once more if the stock price reaches above \$25. Adding on to this, \$11 will not be the ideal price but a logical price; do not be surprised that the stock price drops below \$11, and remember, this investment is more of a gamble than other investments.