Rodney's Take

February 13, 2023

Dwindling COVID Cash and Letting the Freak Flag Fly

Between Uncle Sam and the Fed, the government doled out roughly $10 trillion during the pandemic to stave off economic calamity. About half of the cash went to individuals, as more money found its way into people's pockets via their employers and businesses (think payroll protection). As we spent the windfall, we drove prices higher on goods and services that were available in limited supply, which fed inflation. We've now had some time for the cash to work through the system, for supply chains to catch up and normalize, and for the demand balance between goods and services to swing back toward equilibrium. In short, the froth is coming out of the economy, and that's a good thing, but it might not bode well for investors in the short term.

The Fed remains hawkish, our COVID cash stash is dwindling, and the markets have soared since the first of the year. That's a recipe for negative shocks in the very short term, but there's a way to play this scenario: get naked.

J.P. Morgan Asset Management estimates that personal excess savings peaked around $2.1 trillion in 2021 and then fell to $900 billion at the end of 2022. At first, consumers were using the extra bucks to pay for the rising prices of goods and to pay down credit card debt, but those days are over. Now, revolving debt is expanding, even as more money drains out of households. While average weekly earnings are growing at about 5%, that's not enough to keep up with inflation at 6.5%. Considered altogether, this

points to slower consumer spending in the weeks or months ahead, which will be a headwind for the economy. But don't tell the Fed.

Last week, Fed Chair Powell reiterated his comments from the press conference that followed the central bank's latest monetary policy meeting. The bankers see that inflation is decelerating, but that is not enough to sway them from raising rates at future meetings. Notice that Powell spoke about raising rates not just at the next meeting, but at more than one meeting. Just as they did after the press conference, investors last week disregarded the Fed's clear intentions and sent the markets higher.

Maybe we'll just keep going. Perhaps the algos are right, and the central bankers will see the error of their ways before the March meeting and take a pass on raising rates. Or maybe not.

With growth stocks on fire this year and names like Tesla up 100% from the low, this seems like a bad time to go all in on the next great bull market. An alternative is to find the names you would like to add and, instead of buying them, sell naked puts. As I write this, Tesla, Inc. (Nasdaq: TSLA) is trading at $199.50 per share. You as an investor could sell the $190 puts of February 24 for $6.90, which is almost 3.5% in less than two weeks. If Tesla stays above $190, you'd keep the $6.90 premium you collected. You're ahead of the game as long as Tesla stays above $183.10 and below $206.40. The only problem with this is that at $200 per share, you must be ready to spend $20,000 on TSLA if you get exercised. Still, if you're looking at stocks like Advanced Micro Devices, Inc. (NYSE: AMD), Nvidia Corp. (Nasdaq: NVDA), or even Amazon.com, Inc. (Nasdaq: AMZN), it's worth checking out the put premiums to see if you find them enticing. The worst you can do is end up owning a stock that you were already considering, but at a much lower net price if the markets roll over as the COVID-cash consumer spending train stalls out.

Rodney

Got a question or comment? You can contact us at info@hsdent.com.