# *Harry's Take*

December 27, 2022

## Reader Mailbag: Questions and Harry's Answers on The Fed, Currencies, Commodities, and Shorts

*We receive many questions on various topics, including direction of the markets, demographics, and interest rates.  From time to time, we gather a series of questions on a topic or two and send them to subscribers as part of our Reader Mailbag series. Reader questions may be edited for clarity.*

**Q:** It looks like you were right about a lot of stuff. About real estate, I have some ranch land that I have been offered a ridiculously high price for... about seven times what I paid for it 15 years ago. Half of it is in plantation timber, but it would never be worth a tenth of what I could sell the land for. Right now, the only thing I get to do is pay property taxes on it. I am thinking of selling it, but tangibles may be worth more than cash. I know you have arguments with gold bugs, but it is becoming more evident over time that the fools running the country are going to destroy the dollar and the "reserve currency" label may be lost. The new Petrodollar may be based on a basket of commodities, with China and others in control. In that case, the U.S. could no longer print all of the money it wants and would have no control over other countries and currencies as they do now... having lost all leverage. If this is inevitable, do you see this happening sooner or later?

**A:  The history is that the dollar will rise in a crisis like this one, as it did in 2008. I see that happening, and then the dollar will fall longer term and Asia will become more dominant. I know it's popular to believe that the dollar will lose its value suddenly in a crisis, but 2008 proved otherwise. It's best**

**to invest in the 30-year U.S. Treasury bond, which locks in higher rates before they fall and which is based in the U.S. It is not that the U.S. is in good shape, it's just the best house in a bad neighborhood. Note that we'll see the fall you are talking about over time from around 2025 forward.**

**Q:** What is the best way to short the Nasdaq?

**A: There are two easy ways to short the Nasdaq, but they play on the Nasdaq 100, which is just slightly different. For the Nasdaq 100, QQQ is the largest and most tradeable ETF for betting on the bullish side and TQQQ is three times long. But for shorting, which is the play now, PSQ is an ETF that is simply one times short QQQ. The SQQQ is three times short QQQ. So, it's your choice how much leverage you want. I like the SQQQ to short for a minority position in your portfolio, and then you also should have ZROZ, an ETF that is an average 25-year Treasury bond play. This gives you some diversification in a time when there are few things that do well. The PSQ or SQQQ will tend to do better in the earlier stages of the crash, like January 2022 until now and likely into this third wave down that's forming. Treasury bonds, ZROZ, and TLT (ZROZ about 1.6 times leverage) will do the best toward the end of the crisis when they become the only safe haven... after even gold goes crying to mommy.**

**The best short play I see would be something like 20% SQQQ (equivalent to 60% short QQQ) and then 40% or even up to 80% ZROZ, which is less volatile. Then you would switch increasingly out of SQQQ into ZROZ after it looks like the third wave down that appears to be starting is completing sometime next year. The ZROZ and TLT ETFs should light up like a Roman candle near the end of this crash of a lifetime, as in the second half of 2008. So, you'd want to end up with more like 80%+ ZROZ or TLT, probably. My guess is that the final crash crescendo would be in the first half of 2024, but this is an unusual downturn, given so much central bank manipulation. It could come in late 2023 as well.**

**Q:** What are your thoughts now about both direction and timing for oil and precious metals?

**A: Both oil and precious metals are economically sensitive, so both are good to short in the crash. But gold will hold up better at first, because it is**

**perceived as a safe haven. That will fade fast as the economy quickly gets worse, as happened in the second half of 2008. I think it's better to be selling gold now rather than waiting. Gold will not be the safe haven, as it was not in 2008!**

**Q:** The Fed will be technically insolvent within weeks. It comes up with a kind of magic accounting trick to fill the gap in the balance sheet with so-called “Deferred Assets,” an IOU for future profits, booking future profits now as if they already exist, making it seem to the public that it is not insolvent.

The Fed now has more than $13 billion USD in these deferred assets (booked as “earnings remittances due to the U.S. Treasury”). That’s after two or three months or so of quantitative easing. On the other side of the balance, they only have $35 billion USD in capital and equities. Going forward like this, in a matter of weeks it will be insolvent. And printing more money would make things even worse (with even more negative equity). So now my questions are: Don’t you think this will lead to a loss of confidence from the public in the debt market sooner rather than later? And what does this mean for TLT and ZROZ?

**A: Frankly, I don't think the public is that sophisticated. It doesn't really matter what the Fed's balance sheet is, as it is an artificial entity that creates money out of thin air. We have to work to create GDP. What matters is the Fed’s impact, and that has been to keep a slowing economy growing for 13 years by printing massive amounts of money that created a massive financial asset bubble—and not CPI inflation as feared, until recently after the overreaction to COVID. Many were worried about inflation from such money printing. But the inflation came mostly in financial assets. It is the collapse of that bubble that the Fed largely created by overstimulating our economy for 13 years, especially after COVID, that will kill the Fed and all central banks, along with their credibility.**

**The first bubble was more natural, with strong demographic and technology trends boosting spending and productivity. This second bubble, meant to head off the next Great Depression, was 100% artificial, and it will have a bigger collapse than 2000–2002 or 2007–2009 in a now demographically weaker economy. The economy will go through a shorter but more-brutal depression as this bubble bursts. Two hundred and fifty**

trillion dollars to $300 trillion will disappear from a $600-trillion global financial asset bubble that was led by China and the U.S. but occurred everywhere and that included even more money printing by the EU and Japan relative to their economies. China did something worse: They printed condos instead of pure money; now, 22%+ sit empty. That's a deflation crisis all on its own.

When the crash happens and half of the $600 trillion in financial assets suddenly disappears, it will create both deflation and deeper bank failures than a normal recession. Debt and mortgages in particular are how we create the most money out of thin air. The artificial Fed and central bank injections and interest rate reductions encourage and make it easier for such asset bubbles to inflate.

Banks largely lend against financial assets and their cash flow. When both collapse, loans fail, and banks only have about 10% or so reserves for that. That creates major bank failures in addition to high unemployment and business failures. As in 1929–1933, these financial asset collapses are called depressions (instead of recessions) because of deflation throughout the whole system and because huge amounts of financial assets and future spending power disappear from the system for a long time. While the whole system deflates, the largest impact is when financial assets come back down to fair value. That takes a lot of money out of the system and causes lower spending by consumers and businesses near term, and longer term to a lesser degree. Would you spend less if your net worth suddenly dropped by half or more?

This crash will be global, and it will be the worst since 1929–1932, but the U.S. will come out as the best house in a very bad neighborhood compared with our biggest competitors: Europe, China, and Japan. Southeast Asia and India will be the biggest winners after the crash, as they have the least debt exposure and will grow the most demographically in the future in Asia, which will be the most-dominant growth area in the next boom and for decades to come. The U.S. will have one last fling of growth with the Millennials into 2037, and then will start looking like Europe and East Asia now do, with much slower long-term growth. Increasingly, the future belongs to the emerging world, most especially the southeastern and southern (India and Pakistan) parts of Asia. North America, Northern

**Europe, and Australia/New Zealand will be the strongest parts of the developed world in the next global boom from 2025 to 2037. Only "Oz" will continue to grow after that, and only because it will get high levels of immigration from Asia...**

**My sincere hope is that the Fed and central banks will lose so much credibility from pumping up this insane, artificial bubble that they will lose most of their power in the future. They should be seen as creating more harm than good and should be relegated just to keeping the money supply adequate to facilitate natural spending growth... with NO MORE micromanaging the economy by pretending they are smarter than the markets about setting interest rates and asset prices!**

**Q:** It seems ZROZ is not going higher in spite of the current uncertainty. Is this still normal? Is this still a hold with the current, maybe short-term recovery and the fact that rate increases might slow down as well as inflation?

**A: The ZROZ ETF is up as much as 32% since its low in October. It is definitely a hold. It's just taken longer than in the past to see the deep downturn ahead past the stubborn and/or still rising inflation at first. But that inflation is finally falling and will fall much more ahead.**

**Q:** Should not the Fed's continuing sales of longer-term Treasuries and Mortgage-Backed Securities (MBSs) at the rate of $90 billion/month result in much higher yields going forward? And would not that outcome weaken TLT's NAV as 2023 and 2024 unfold?

If the answer to these questions is yes, then how does that affect your strong recommendation that we buy TLT for the expected crash in equity markets?

**A: God talks to me through charts, which reflect all of this info and what is known. The TLT chart looks like TLT put in a major long-term low at 91.85 recently. What I am betting on with TLT and ZROZ is that we're going into a recession, which means yields will fall and T-bond prices will rise, as present rates are locked in higher for 20 years. It's that simple. If we don't go into a recession, then that may be a bad bet. If TLT breaks to new lows, then I will**

**have to reconsider. I'm looking good so far on this bet. The Fed's actions, past and expected in the future, are taken into account here by the markets.**

**Note that it is worth taking some risk in this period and holding through some short-term volatility, as I am projecting that TLT could nearly double to 196 or so. That would be the biggest move in history and likely for decades ahead. You don't get that level of reward without the markets trying to talk you out of it at first...**

**So, don't let the markets talk you out of it here!**

**Q:** CNBC and Fox never mention a "bubble" but do refer to a possible mild recession in 2023. What do you think Powell has up his sleeve?

**A: All government and Fed officials always minimize forecasts of a recession, and then when it becomes obvious that we are moving into one, like now, they always say that the recession will be mild. There's no way to have a mild recession after a bubble this large and pervasive: $300 trillion in financial assets has to disappear. There's no way to do that without pain.**

Harry

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