Harry's Take

February 28, 2023

Reader Mailbag: Questions and Harry's Answers on Real Estate, Currencies, Rate Hikes, and More

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: Will the Chinese in their coming real estate crash move their money to our real estate market and make our market go higher?

A: This will be a worldwide real estate crash after a worldwide bubble. There will be nowhere to hide. China's real estate will go down as much as 70%; ours will go down as much as 50%. People aren't going to want to buy anywhere for a while, and that's why real estate will be much slower to bounce back than stocks. Stocks took 17 months to reach the bottom in the 2008 crisis. Real estate took six years.

Q: Is there any chance that the price of Bitcoin has reached the bottom of its four-year cycle?

A: It is possible that stocks and Bitcoin bottomed in late 2022 on the four-year cycle, it's just unlikely. We have to remember that central banks have been intervening since early 2009, pumping up the first totally artificial and everything bubble in history, which obviously is able to throw off credible cycles like this one. The natural cycle forecast a recession or depression from late 2007 into late 2022 (like the long depression between

late 1929 and mid-1942) and a final crisis between late 2019 and late 2022. But it appears to me that the beginning of the crisis may have shifted to late 2021, and it could continue into mid-2024 or a bit later… It's that simple!

Bitcoin normally bottoms about a year or a little more after its four-year cycle peak. But this is actually a series of three-year or four-year cycles that build into a larger top over 12 years. Thus, it should take longer to make a bottom, and that now is likelier to happen in late 2023 through mid-2024+ instead of in late 2022 after a late-2021 top.

Q: REIT positions will continue to pay out dividends, even though the market is declining and share prices are falling. Is this a sector that would be okay to stay in?

A: REITs are an interesting sector! Beware of commercial office space REITs. They always get hit hard in a downturn, and the remote-work transformation is putting pressure on this sector. One group estimates that values will fall by $450 billion as large corporate tenants reduce their square footage in the years ahead. If this is anywhere close to correct, then the price per square foot will fall, dragging down dividends, and market value will fall. There's a reason that Blackstone had to cut off redemptions from its commercial property REITs. Those REITs that focus only on multifamily/apartments will hold up best and will pay those dividends while they do. I would still take a 30-year Treasury bond over that any day during this crash period and into 2024 or so. Commercial REITs should do best in the next boom from 2025 to 2037 and should fare better than multifamily, as the Millennials will peak in that area on a 26-year lag by 2026.

Q: After the latest Fed rate hike, did you hear anything to change your mind about the short-term direction of the markets?

A: I see no real changes, just much more downside still likely ahead. The Fed is trapped. It started to edge off to lesser tightening with 25 bps, but now a strong jobs report means it either has to stay at 25 bps for longer or step up to 50+ bps. The markets never bottom when tightening cycles are still in motion.

Q: I would be very interested in what you recommend your subscribers do when already short positions with, e.g., SPXS or SQQQ are running. Do you now simply hold these positions (also the 3x short positions) until the third wave hits, or would it be better to close the positions with (considerable) losses?

A: At this point, people holding short positions should just keep them, as the markets aren't likely to bounce a lot more from here. It does tend to pay off if you sell after a large downturn, as into June or October 2022 after the first-wave crash. If this next wave breaks downward, as confirmed by new lows below 10,088 on the Nasdaq, then I will be warning you when it looks like the next third wave down is bottoming near the 2020 COVID lows. That would be a time to take profits and short again on a substantial bounce.

Q: I am wondering what your thoughts are on the current wage inflation and to what extent it is driving overall inflation. My suspicion is that two things are occurring. Baby Boomers are exiting the workforce due to retirements and/or expiration, and the ones who are still working are well past their peak efficiency, as you point out frequently. Taking it a step further, those inefficient Boomers still in the workforce are having a hard time finding people willing and able to come do the work they can no longer efficiently get done.

A: Yes, we have a situation here where a lot of aging Baby Boomers left the workforce during COVID, and some are close enough to retirement just to decide not to come back and instead to retire a few years early. That keeps the workforce tight and plays into short-term inflation. Inflation should back off pretty quickly when the economy slows ahead, and crashing stock prices, which are likely to continue, will make the upper 20% in income that drive 50% of spending more cautious, as they own almost all of the financial assets. These assets will continue to fall and will not come back to previous highs ever, or at least not for a decade plus. The downturn will take pressure off of the labor shortages, as the Millennials are not quite large enough as a group to offset the larger group of retiring Boomers. After the bust, inflation will remain low, as workforce growth will be slow, with Boomers continuing to retire into 2042. The new, younger group, the Millennials, also will boost productivity, as older, less-efficient workers are

replaced by younger ones who are moving up their productivity curve rather than having plateaued.

Q: I have not really had much experience with bonds, but I do understand that when interest rates drop, the bonds with the higher rates become more valuable. I am asking if you would go into more depth about how it works. What is the interest rate now, and how much does it need to drop to produce the returns that you are predicting? Is there an exact correlation to rates and bond value, or is there a set of general rules about how much they change? How much does the demand for bonds affect the price? What could bring about another move against down?

A: Interest rates on the 10-year Treasury bond are at about 3.90% on the 10-year and only slightly higher on the 30-year. As the economy slows and inflation falls, those rates could plummet to as low as 0% on the 10-year and 0.5% on the 30-year. They previously (in 2009) fell to as low as 0.4% on the 10-year. Your present T-bond will appreciate a lot more if the economy slows and rates fall, as you have locked in that 3.93% or so rate for 30 years instead of for 10 years. Longer duration equals greater appreciation.

Q: Do you think that if the paper U.S. dollar disappears, digital dollar currency will have a detrimental effect on investing due to government control?

A: If the paper dollars disappear, then digital dollars will be easier for the government to track, and that would make it harder to hide money or revenue when people pay in cash. Otherwise, there's no big impact. You can see why the government favors digital.

Q: In reference to Harry's Take, February 14, 2023, at a glance, there appear to be far more false sell signals on this chart than valid sell signals. How do we ignore all of those false sell signals now?

A: In almost all cases, the markets went sideways to down slightly for a while, even if a substantial crash did not follow. But the way I discriminate is by looking at similar times, i.e., what's happening now, after a substantial crash, has begun to look similar to what happened in 2001 and 2008. That's what the two dots highlighted and what they now have in common. After a

major bull market or bubble when a larger crash could be warranted, this becomes more important to compare, and that's how the present dot lines up compared with the two highlighted ones in the chart. In short, I am highlighting a similar period, and that's where it should most line up.

Q: Do you have thoughts about how low TLT will go? Do you recommend holding?

A: I still think TLT bottomed at 91.85. It's best to hold unless TLT breaks that. The potential rally to $186+ is huge—potentially the largest in history, either past or future, and is worth taking a little pain for.

Q: A Fed of New York statement on Tuesday, November 15, 2022, announced that Global Banking Giants and the New York Fed are testing the digital dollar in a 12-week pilot. Will paper money be worth less? What's your opinion on gold?

A: The U.S. dollar is still the global reserve currency and the best house in a bad neighborhood. I see the U.S. dollar appreciating during this crisis, as it did into late 2008, because the present downturn likely will continue well into 2024. Then, the dollar will fade into the next boom as Asia continues to rise in influence. Gold is the opposite. It will turn down into the worst of the crisis, as it did into late 2008, and then rise during the next global boom, more due to the rise in India for decades to come, as India will be the "next China." Indians love gold for jewelry. So, gold will rise toward $3,000+ in the next boom due to fundamental demand, not for monetary reasons. Paper money increasingly will be replaced by digital transactions but will not disappear, and that transition will not affect the value of money. Money doesn't care if it is paper or digital.

Q: Is 4.00% on the 10-year Treasury a particularly significant level?

A: The highest yield recently was 4.5%. After this tightening cycle has begun, yields are unlikely to go back that high; hence, around 4% could be a stopping point for bonds. TLT bottomed at 91.85 in early October 2022. Around 99 looks like the best place to add or buy, if you haven't already. That will be near that 4% level, and round targets like that will tend to create resistance. Hence, they are a good place to top. I see the TLT target

as the better one, and that could come soon, given that it hit 100.56 on Friday. It doesn't matter what or how you are buying, whether direct 10-year or 30-year bonds, ZROZ, or TLT. Use the target on TLT near 99 as the buy signal, although you might target a little higher, like 99.5, to make sure you don't miss it.

Harry

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