Harry's Take

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Reader Mailbag: Questions and Harry's Answers on Inflation vs. Deflation, AI, and Bitcoin

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 and answers on a few topics and send them to subscribers as part of our reader Mailbag series.

Q: Won't the election-year politicians do anything to keep markets rosy until it's over? I mean, nothing happened until Obama was elected, and then the air came out of the tires! I just don't trust these politicians who control the strings.

A: Yes, markets tend to lean positive in election years, but the Fed was forced to raise rates 525 bps into July 2023, and the effects of that will keep hitting harder into early 2025, just past the election. The Fed overreaction to COVID by means of stimulus caused the 9.2% inflation that forced this tightening. Otherwise, the central bank wouldn't normally tighten like this before an election year. The federal government does not have any direct control over the Fed.

Q: With this new wave of AI entering the present and future markets and potentially taking jobs away from humans in developed and, most importantly, developing countries (India and those in Southeast Asia) that you have forecast to have strong markets in the future, how will AI affect the demographic trends that you rely on for market structure and forecasting?

Will your demographic data and the economic forecasting be skewed or become less important due to AI?

A: New technologies always alter or eliminate many older jobs, but ALWAYS create more new and better ones. AI is the next step in my 45-year Innovation Cycle. One of the big trends I see is putting better information in the hands of front-line workers, to allow companies to better meet their customers' needs, with measures of profit contribution down to individuals and with small teams to pinpoint and deliver compensation and bonuses for real contributions. More everyday workers and small teams will become like small business units within larger companies, with their own profits and losses. It will be powerful to measure business accountability in real time.

Henry Ford ushered in the assembly-line revolution from 1914 forward, which led to a similar surge in the productivity of everyday workers. Did jobs disappear and kill the economy back then? New technologies improve everything and create a bigger pie for all! They are a vital part of the three-cycle hierarchy that drives our economy. The Innovation Cycle actually is weaker into 2032, simply because the Internet is moving into full maturity. Most leading-edge tech sectors like AI and biotech will have the biggest impact down the road, from like 2032-2055.

Q: What is your prediction on the Australian housing market?

A: Australia does not have the demographic weakening that North America and Europe have, but they do have an even more–extreme real estate bubble. I expect Australian real estate prices to fall by 50%, similar to the U.S., and that is what will hit your economy and consumers. The difference is that in Australia, real estate will have a shot at new highs in the next global boom into the 2050s, whereas in the rest of the developed world, it will not.

Q: With historical trends consistently showing an 18-month rally after a Bitcoin halving, you have multiple signs indicating instead that we are reaching a major top. Were these signs not present to this extent previously in the past halving milestones and would you not have predicted a similar scenario, or are other factors now in play?

A: I track Bitcoin like a hawk, partly because it tends to lead stocks and partly because it's the leading edge of risk assets, with AI now up and coming. The four-year cycle should peak in late 2025, as in late 2013, 2017, and 2021... But I am starting to think that peak is so anticipated now that it may not play out as nicely as in the past. It is not clear whether Bitcoin is in a 1 wave up of a new, larger 3 wave up or in an irregular B wave of a 2 wave down. I will be commenting on this as it unfolds, but it's certainly not clear yet. In the B wave of 2 wave scenario, new highs should not go back above $73,600.

Now that Bitcoin has broken to new highs well before the four-year cycle has peaked, as is expected in late 2025, my new targets for that time frame are $140,000+, unless we get a big crash into late 2024. The latter looks less likely now but still is possible and is more in line with a likely larger stock crash, given that the second bubble looks to have peaked between late 2021 and early 2024.

Q: Both the Nasdaq IXIC 100 and the Nasdaq Composite NDX have broken to new highs and are going strong. I can't follow your numbers on the Elliott Wave graph. Where is resistance on any Nasdaq chart? March 12, 2024, was not the high. Can you explain?

A: There's no real resistance, as the Nasdaq is making new all-time highs. But since late 2022, we clearly have been in a broader and likely fifth final wave advance, and now the final fifth subwave should be looking to peak. A top looks possible on March 28. There's no way to pick it perfectly.

Q: What about a **stagflation** scenario, Harry? Interest rates could conceivably rise from here if inflation reignites, which looks entirely possible at this point. If that happens, our TLT/ZROZ positions will be screwed! What would be the strategy then?

A: TLT is for playing a slowdown. If that does not happen soon, we'll get out. The Fed is determined to slow the economy and inflation, so I don't see how inflation will come back; if it does, the return would be brief. Remember that the 525-bp hike into July 2023 does not fully hit until early 2025!

Q: If there is inflation and the Fed is not going to pivot, how will TLT rise?

A: TLT rises when people perceive the economy to be weakening with falling inflation. That would lead to lower long-term rates, which would lead to a rally in risk-free bonds. This is the clear intent of the Fed, and its 525-bp tightening will hit harder as we move into early 2025. A slowing economy is bad for stocks and earnings and for most bonds as default risk rises. It is good only for risk-free Treasury bonds, on which the government will not default and which benefit from falling inflation.

Q: I have wondered where we will head next, deflation or hyperinflation, given what is happening with globalization. As I understand it, the following happened in the past: as globalization 1.0 broke down in the aftermath of World War I, the world's factory (the U.S.) suffered deflation, while the biggest account deficit nations (those of Europe) suffered severe inflation and a few hyperinflations. China is the factory now, and the U.S. has the big account deficits. So, it will be extreme stagflation/hyperinflation or deflation. Your thoughts, please.

A: Deflation will come once this second, larger bubble bursts more fully, likely into early 2025 or so, and it should linger some. After that, inflation should be low in the next boom into 2037. We'll not get hyperinflation, to Peter Schiff's disappointment, unless central banks go crazy and double or triple down on the money printing, which is not likely, since the last double-down obviously failed.

Q: Can you explain why TLT will be a good place to park money if the Fed will be lowering rates?

A: The Fed only changes short-term rates. TLT is an average of 30-year and 10-year Treasury bonds (so, an average of 20 years). The tightening of rates from March 2022 through now and remaining at 525 bps through at least June point to a slowing of the economy for up to 1.5 more years. That slowing would bring down longer-term T-bond rates, which would make bonds go up in value from the higher rates being locked in now.

The lowering of short-term rates a bit that is expected around June or later will be more likely if the economy is slowing; such slowing is good only for long-term, risk-free bonds, which have no default risk in a recession. Rates

usually are lowered only when the economy is already in recession, and the effects of any stimulus take 1.5 years to hit fully… See the trap the Fed's in? This is another reason it's dangerous to interfere with the natural forces and cycles.

Q: Do you think all the alt coins will follow Bitcoin? I own some Ethereum and want to protect the gains I have made thus far.

A: **The whole crypto sector will go down, as Amazon and the dot-coms did in 2000-2002. Bitcoin and Ethereum are over half the valuation of the whole sector! I prefer playing them!**

Q: Do you have any recommendations on the best ETF to short the Nasdaq like the SPXU is for the S&P?

A: I like PSQ single short and SQQQ triple short and higher volume than PSQ; these are good fills in tight markets. I like SQQQ with T-bills to bring risk down to desired level or more toward PSQ, due to the high volume.

Q: Is it safe holding SQQQ long term while waiting for a correction? Many advise strongly against it, but we've been at it awhile. I hate selling now at a loss if holding is okay. I'd hate to miss the correction.

A: As for holding, I'm not talking long term here, only for likely 1-1.5 years. A slowdown remains likely this year, up to a point. So, it's better to hold SQQQ and TLT, as they will shine in a crash. That crash is long overdue and is looking increasingly likely, as the effects of tightening should hit the strongest into late 2024–early 2025. If stocks don't start to head down by June, then I may have to reconsider.

Harry

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