Harry's Take

October 2, 2024

Reader Mailbag: Questions and Harry's Answers on the Fed, Real Estate and the Markets

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: What capacity does the Fed have in creating a softer landing as the global economy slumps?

A: The Fed can only lower interest rates and inject money into the bond markets to support financial assets and the economy a bit. If consumers and businesses get scared of a recession, that will tend to overwhelm the easing policies. It's hard to forecast when things start to fail enough to generate fear in investors, but a correction over 20% is a good start. But even that occurs often enough, and you are getting out guaranteed already 20% down. That's why it's best to be safe and in safe haven investments like Treasury bonds when markets are this overvalued and stretched so long without a bona fide recession, until the trend becomes more clear to the downside, and then you simply hold those until there is a serious crash and investors are no longer bullish. I think the downside trends are now much more likely after 15 years of a nonstop bubble (except COVID very briefly).

Q: You wrote a book in 1989 called *The Great Boom Ahead* about the spending patterns of the baby boomers which were going to peak at age 47. I ran Scott and Stringfellow and patterned the success of the firm in the late

90’s after your premise and it turned out to be true. We sold the firm in 1998 at a nice multiple to book.

I got you to speak at the regional firms annual meeting and it was well received. In today’s world are not the Millennials replacing the Baby Boomers and they are much larger in number? They are amassing debt and spending like there is no tomorrow so might not that delay your timing on the bubble bursting?

A: The Millennials are just kicking into their Spending Wave starting in 2024 and hitting a peak around 2037, but then a long plateau into around 2055. Their Spending Wave is not nearly as steep as the Baby Boomer’s was. There are more, but they started at higher births, do not advance as steeply, and hence will not be as impactful overall. Their long plateau from 2037 to around 2055 (with a modest break into the early 2040s) will be very unusual in history. Demographic trends don't tend to plateau like that except in a late maturing trend. And that is what 2007 to 2055 is for the U.S., a long maturing plateau. After that we literally decline, like Japan since 1996, unless we maintain or increase high immigration. It is very difficult to get aging affluent populations to have more kids.

Q: How can we tell if we are currently in a recession?

A: It's hard to tell and most reports around GDP, etc. come out on a lag, and are endlessly revised. They make the downward revisions later and they are not noticed that much. Better to look at GDP trends and consumer and business sentiment.

Q: Still looking for a crash? I sold 700,000 of gold stocks several weeks ago. I’m down about 250,000. Not blaming you. Just life in the market. Problem is I owned gold stocks for 8 years. Sold looking for the crash. Unfortunately it looks like the market is up.

A: No question this is the most pushed off crash in history. Now 15 years since the end of the last recession, the longest in history of markets and by 50% over even early 1990 to early 2000. But paradoxically, the longer this first 100% artificial bubble goes, the higher the odds of a crash, and a greater one.

Perhaps the best approach is to be short stocks starting at just 10% of your portfolio and increase that 10% or so each month until markets start to turn down more sharply, then add more shorts more rapidly as it goes down until you are as short as you want to be.

This has been the hardest bubble ever to short due to government support for it… but I still fully believe: the bigger the bubble, the bigger the burst when it finally happens. It is also hard to pick a bottom, and the smart money tends to edge into that similarly. A very successful investment mentor told me that he focuses on getting the middle 80% of a move, as the first and last 10% are the trickiest. That's when there is a bull/bear war until one side starts to win, and the new trend is more playable.

Just to go back to late 2022 lows now would cause a 45% crash on the Nasdaq 100 (QQQ). And then that qualifies for the first wave down of a larger 80%+ crash overall.

Q: If the Bric countries are successful and dump US Treasuries next year, what will happen to TLT?

A: That's hard to see and why I look more at chart patterns. The smart money anticipates a lot ahead, so you are not likely to be ahead of them on issues like this. Also, the Treasury bonds are the largest and most liquid market in the world, hence, BRIC buying on its own is not likely to impact the markets that much. And the BRIC emerging market countries are not as big an influence in stock markets as the affluent investors in those countries, and more so the "smart money."

Q: I don't get it. The Fed makes a 50 basis point interest rate cut and TLT goes down? I would have expected the opposite. Is this a scenario of buy on rumor and sell on news or a sign that TLT will not go up as interest rates go down?

A: First, this was already heavily anticipated and priced in. These rate cuts have been the most telegraphed in history. Second, lowering long-term rates for consumer and corporate borrowing makes housing, cars and business expansion more affordable and that causes higher spending which stimulates economic growth, which in turn tends to cause higher inflation. The bond markets here are seeing lower rates to be more expansive, and hence, inflationary. Tightening, by raising rates, causes the economy to

slow, and hence inflation, and hence lower longer-term bond yields, which makes T bonds go up in value. In recessions from slowing the corporate bonds may see lower inflation, but they also see more defaults, which makes their bonds go down in value from higher risk. The T bonds have NO default expectation as they can print money to pay them no matter what, unlike corporations. That's why they go up in a down economy, while corporate bonds can go down despite falling inflation which would otherwise be good for their bonds.

Q: I've been following you for decades. Following your advice in December 2022 I sold off most of my stocks and went into your recommendation for a position in TLT and ZROZ . I have been at a loss ever since. I've certainly missed out on a lot of gains that my sold stocks achieved over the two years.

As these two defensive plays slowly approach a breakeven point for me I'm concerned that your forecasted "crash of a lifetime" will take these two down 50+% with the market and I'll be back years to recover. Should I sell these two holdings to wait out the crash and then buy them back? Is SQQQ still something to move into at the start of the crash to avoid the crash drops?

A: Sorry to hear that... Ditto for me. This has been the trickiest bubble and top ever due to massive manipulation. There is no precedent for this. But one thing for sure: This greatest and longest bubble ever has NOT burst yet. There is no way you can bubble up the economy and stocks so far above what would have been a 15-year slowdown from 2008 - 2023, and not have major consequences and a reversion back to the mean. TLT has been up since April and should continue. Stocks finally look like they are peaking now… best sign of that would be if Nasdaq can't follow S&P to new highs near term after the Russell 2000 has failed to for 4 years now.

Best to hold the course: short stocks, long T bonds. Most conservative, just long T bonds. If we don't see signs of the past tightening by the first quarter, then I am going to have to reconsider. That's when the tightening should hit more fully. If you are not willing to take some pain for the biggest long term T bond rally in all of history, then be in cash/T-bills until trends are more clear to the downside. You will miss a good bit of the gains, but you also will not be beat up in the meantime. The smart money is willing to take a trade like this when it is inevitable and hold until it manifests. Most investors chicken out too early.

Q: Commentators like Peter Schiff and Mark Moss are calling for a reverse crash. They believe that inflation will continue to blow up and markets will go higher as the Fed cuts rates. Schiff predicted that the long bond rates would rise after the Fed starts cutting and that is what we saw this past Wednesday. He thinks that we just put in the low for bond yields as inflation begins to come back in. I'm heavily invested in ZROZ and TLT as you have recommended. I'm concerned that the reaction of bond yields on Wednesday suggests Schiff is correct and ZROZ and TLT will continue downward. Your thoughts?

A: Has inflation continued to blow up? It's fallen from 9.1% down to 2.5% - 3.0%. Look at the 2008 debt and financial crisis that was cut short by massive stimulus. Did we get rising inflation or falling? The 10-year Treasury went down to 0.4% yield and appreciated near 50%. A crash ahead from this unprecedented debt bubble can only be deflationary as debts failing and being restructured destroys money that was created from over-expansion debt and money printing - and that is deflation!!! Not inflation. Hyperinflation only occurred seriously once and that was when Germany in 1923 tried to inflate its way out of the massive WWI war costs and reparations to follow. This is not that! This will be a debt deflation as such debts fail increasingly in a falling economy, like the 1930s... again deflation!

Schiff and Mark Moss will be right about a debt crisis ahead, but DEAD wrong about hyperinflation to follow... unless Europe and the U.S. decide to print 100s of trillions. That would not be allowed by the markets in these times. Germany was desperate and had no options but to print money until they blew up. T bond rates would soar if we ran massively higher deficits or printed massively more money, and make already high non-stop deficits far worse, as will the financial crisis. The U.S. Treasury bonds will be the safe haven, not gold, as was the case in 2008 when gold went up in anticipation of the financial crisis, and then back down when it actually hit fully. If you're not sure if I or they are right, then best to be in cash/T-bills until it becomes more clear. You are likely to miss a good bit if you do that, but the T Bonds tend to make their biggest move towards the peak of the crisis, so you can be late to this trade and still do well. Also, stocks go down in either scenario, just more in the deflation one. So, you can be short stocks until deflation becomes more obvious and T bond rates fall instead of rise and gold falls as well. Gold usually holds up in the early stages as in 2008, but

crashes in the end as in the second half of 2008. Just not as much as stocks. I see gold going back to the $1,100 area or so. Then you can buy for the great explosion of Indian consumers (the next China) who spend more on gold jewelry compared to income than Chinese or Americans. When you are coming from that poor, you like to show off a little wealth.

The reality question to answer: What did better in 2008, the worst year of the last financial crisis: gold or Treasury bonds. It was the T bonds!

Q: What are your thoughts on TLT now after such a big rate cut?

A: They have merely gone from being above the neutral rate of 300bps at 525bps down to 475 with another 75 down to 400 expected by year-end. That is still net tight by 100 bps. They are behind the curve as usual. I am waiting to see how much it hits by the end of the first quarter 2025. If the economy is still buoyant by then, maybe they have created a magic wand. Not my expectation.

The economy should keep slowing and then fall into a recession. TLT wants to see falling inflation and a slowing of the economy. I still expect that. If not by the end of the 1st quarter of 2025, then I re-evaluate.

Q: If crypto markets are a future indicator of equity market direction, is it not OK to continue investing in stocks until the crypto markets lead with a crash? Could you then have the ability to sell equities and have time to invest in long term Treasury bonds, etc.?

Is there a possibility that you could see the crypto market not crashing, even though the equities market would in the future or at least equities could fully crash firstly?

Further, in terms of a hedging strategy, do you think Gold would be a good vehicle i.e. worst case it would retain its value in a deflationary crash, or would you expect gold value to decrease more?

A: Bitcoin has already been down 27%. You can't wait until it's down 50-70% to get out of stocks. The lag has only been around 4 months thus far, and that is what I would expect. The first crash for stocks off a major bubble like this averages 40%. Better to be a little early than late in getting out… and Bitcoin is not bouncing much.

Also Nvidia has been a leader for the leading tech sector, and it is showing stronger signs of downward volatility, another leading indicator that the Nasdaq and stocks should follow. You have to have some patience to make money in investing. Rarely is anyone going to tell you exactly when to get out and back in to catch a bubble top and major crash. You have to take some risk and have some patience to do this. Otherwise, just sit in cash. Don't worry, be happy. And wait to invest again, buy-and-hold when the smoke clears enough.

Q: I am still holding out for the crash like you are. We need to hit the reset button and start all over. The question I had was specifically related to the S&P - What is your prediction for the first wave down? Is it down to 3500, or 2200 or is it a percentage drop, like 30%, or 40%, ...?

A: Average first crash of a bubble like this is 41%, ranging from 28% to 50%. So, it is more a percentage. That would make 3,300-3,400 a good target, but the late 2022 low of around 3,500 would be close to that, and perhaps a better target. But once you see a crash of that magnitude, it is going to bounce a good bit, and then you have to judge when that is over... not that easy.

Q: You talk about TLT being a good hedge for the impending bubble burst. I know it's not about the yield, it's about the safe haven play. But the yield at the moment is 3.68%. What about something like SGOV? It's returning 5.21% Wouldn't that be a better place for now? How would that be impacted when the bubble bursts?

A: The higher the yield, the less the safe haven. And the safe haven will be the only big thing when this damn everything bubble of all time finally bursts. Stick with TLT, TMF or 10- and 30-year Treasuries. Nothing will soar like the 30-year Treasury if we hit a major crisis like 2008, and see this one be 1.5X 2008!

Q: Does your prediction that the price of gold will drop dramatically in the second phase of the Everything Bubble take into account the emergence of BRICS gold-backed currencies in October as well as the massive gold buying by international central banks and sovereign countries? If not, what are your expectations?

A: No, that's already priced into the markets. I'm looking at a global drop in jewelry demand and a general bubble burst, and gold has bubbled along with everything else from stocks to real estate and other commodities in this bubble, up 3.5X since it's late 2008 lows (that's when you buy it at the bottom of a crash). It will go down less than stocks that are up 7.8X since their early 2009 lows (S&P 500). Hence, it's only "less" worse than stocks and likely to go down 50% to 60% instead of 88% to 94% for stocks. There is no clear, sound safe haven for a bubble crash than T bonds - and the longer duration the bigger the gains. That's it. If there was, I would tell you. If someone tells you something else, including gold... they have not done their homework. Not antiques either, or collectibles, or art, or candy bars (that would likely be better). Again, this is not Germany inflating its way out of massive war debts and absurd reparations from World War I that could never be paid from a dead, devastated economy with a lot less men alive to work. The Allies were idiots for doing that out of spite to Germany. Did we do that to Japan after World War II? No, we weren't idiots. And Japan became one of our best trading partners after that, and still is. This is the only real example the gold bugs have -- and it's utter, total BULLSHIT! Not a comparable situation. Period.

The only way it becomes high or runaway inflation is if they go hog wild and print $50 trillion or $100 trillion to counter the deflationary recession -- and the public nor the markets will let them go that far without punishing them, and refusing to buy their bonds. The U.S. is lucky that it has the safe haven status as a country even with record high debts or in a deep downturn like 2008. We have always been able to sell our bonds at a good price. So, don't look a gift horse in the mouth. There is a limit, we haven't tested it yet, and should not even DARE as the biggest borrower in the world! But our government has already pushed that beyond any expectations and it would be very hard to say, we'll just print $50T this time, because $8T last time wasn't enough! Or we'll run 40% deficits nonstop since 6% weren't enough. There is a point where even an idiot can see you can't keep having "something for nothing solutions" and not end up with "nothing!"

Q: Is this a good move because I have been approved to do both. Buy land and or a home anywhere on the gulf coast of Alabama or Mississippi?

A: It's the land that most responds to changes in price. I would not want to buy land now as it should go down the most if we go into a recession next year, as I expect at this point. If I had land that I don't want to sell, then I might as well build on it during recession and get lower construction costs likely during the downturn. Best is to wait and buy a turnkey house at a bargain price a few years from now if we get a crash like 2008. If you want real estate that will generate cash and hold its values better than most that are falling, but affordable multifamily rental properties -- not REITs that focus more on commercial real estate that will fail drastically as usual because businesses have no loyalty to their "house" as many consumers do.

Q: A lot of the recommendations I've heard when it comes to financial investments are more geared toward people who are in total control of their investments. I've played around with buying stocks over the years and I could certainly sell them all and bank the money as a precaution without too much worry.

However, as we head for this crash there are likely many people out there like me who aren't in full control of their investments and simply feed an IRA, 401k or Roth each month as they get paid. As far as I know I cannot take the money out of these accounts without a penalty to put them into a safer place (wherever that may be). I only know that I can call my financial person and ask them to perhaps lower my risk category and that's it. As someone who is not super well versed in the world of finance and the available options, and is closer to retirement than not, what can be done with those types of assets to protect them, or should I cross my fingers the market recovers before I retire?

A: If you can't pull money out of these accounts without penalty, then simply choose the most conservative choices, like Treasury or high quality corporate bonds. If there are only stock and REIT choices, then just leave it in cash or T-bills until we see if there is a major crash. If you have to invest, pick the option with the lowest downside risk, like shorter term higher quality corporate bonds or long-term US Treasuries (the best).

Q: What are the pros and cons of TLT vs TMF?

A: It's simple. TMF is triple short TLT, so it will go down and up roughly three times as much. Most investors should not use that much leverage

unless they are using a smaller amount of money to hedge a larger amount. You can also have say 1/3 in TMF (equivalent to 100% in TLT) and have the rest in cash to pounce on unbelievable opportunities you may just happen to trip on during the crash. Maybe you buy a house down the block out of foreclosure for 20 cents on the dollar when most real estate is down 50%. You have to have cash to do that. You're not likely to be able to move fast enough or get a mortgage loan in a major crash. I was not looking to buy a house in Puerto Rico when I moved here in this bubble, but I had enough liquid investments to buy one for cash that was too good a deal to pass up. And I didn't have to rent in this "bubble that never seems to end." My wife was getting sick of that.

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