MRP CAPITAL INVESTMENTS, LLC

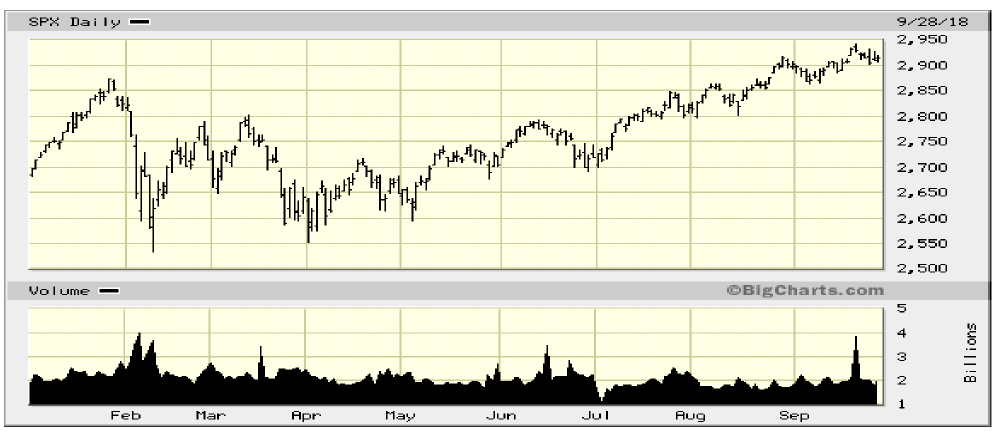
3rd Quarter 2018 Client Newsletter

Capital Market Update

Inside this report:

We seemed to be treading water for most of the year…until this quarter came along. Last newsletter we talked about how earnings were booming, but the market was only going sideways. I reminded everyone that type of scenario creates an under-valued market and it is like a powder keg with a lit fuse; eventually it will explode. And it did last quarter.

As you can see from the chart below, the price change on the S&P 500 was 7.20% for the quarter. And this brings the total price change for the market to 8.99% for the year.



S&P 500 2018 Chart Supplied by BigCharts.com

To be frank I am excited to see more bricks in the Wall of Worry, so to speak. These "bricks" include; Trade Wars, Tariffs, Inflation, Political and Geo-Political uncertainty. It is an old market saying that a Bull Market climbs a Wall of Worry. The basis of this adage is that these worries keep people's capital on the sidelines. The more money on the sidelines means there is more fuel in the powder keg. As investors get more comfortable and move that cash into the market, the market moves higher and higher.

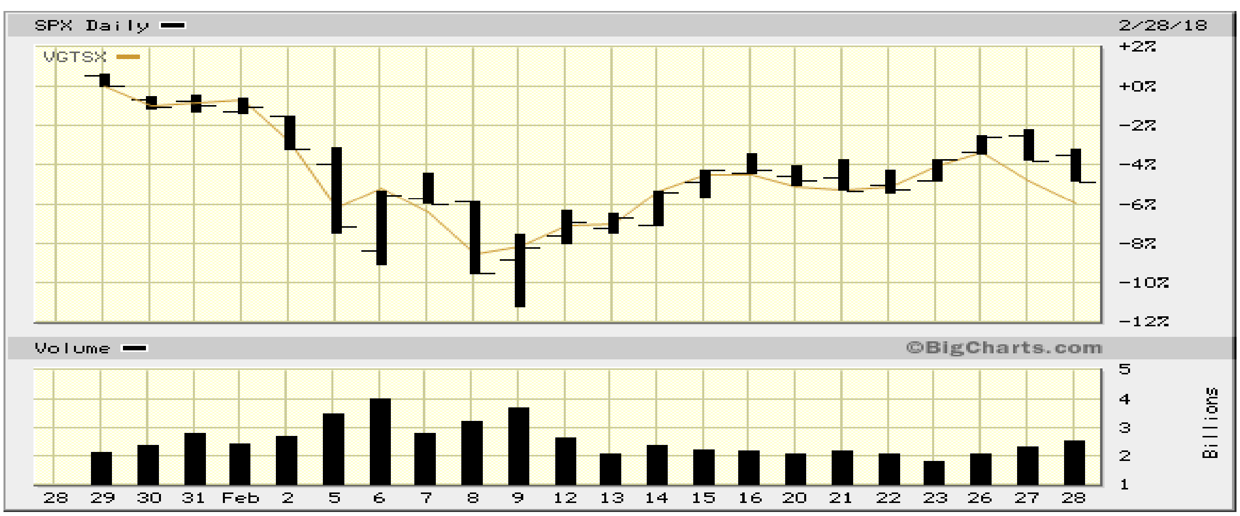
What we need to watch out for is when all the "bricks" are placed and people see no more things to worry about. This leads to euphoria and the end of the Bull Market. We aren't there yet, but we are keeping a close eye on how things develop.

Trade War

In the last newsletter, we had an article entitled "Market Divergence." In it, we noted that the U.S. markets were rallying while most of the international markets had been under-pressure. It was our belief at that time that this phenomena was caused by investors placing bets on the United States "winning" the trade wars. It really seems like that scenario is playing out.

I put winning in quotes because what it seems like is that the current U.S. administration doesn't want to win by punishing our trading partners, rather it wants a level playing field on trade. And that level playing field is plain and simply free trade both ways. As was noted in the Q1 2018 newsletter in the "Tug of War" article, "according to the Federation of International Trade, the United States has among the lowest tariff rates in the world with an average rate of 3%." But our trading partners have made a practice of not being so friendly in reciprocating that low tariff level.

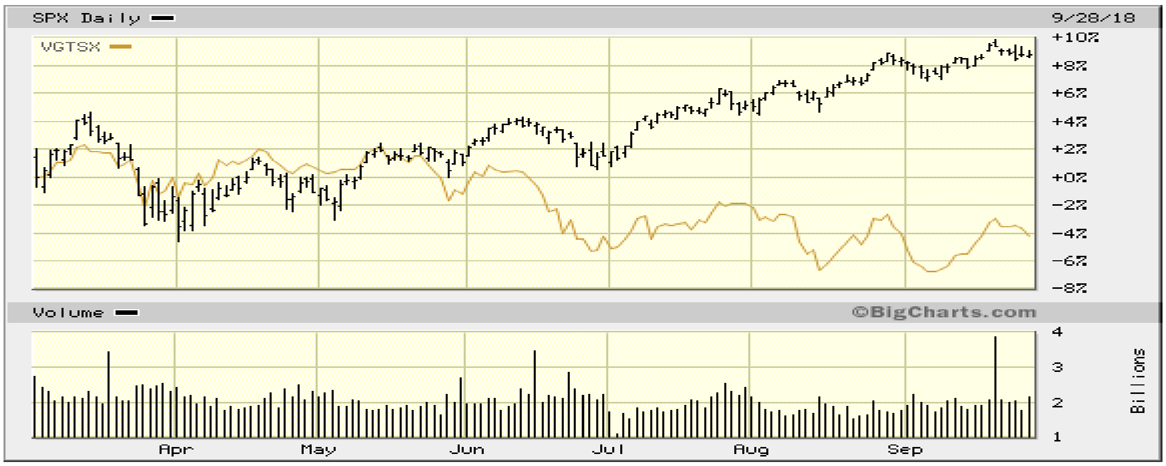
With this in mind, when the Tug of War of trade deal negotiations started the markets were rattled in every direction.



S&P 500 versus the Vanguard Total International Stock Market Index

01-28-2018 through 02-28-2018

Then they seemed to fall into the mindset that the U.S. would be winner in the Trade War.



S&P 500 versus the Vanguard Total International Stock Market Index

03-01-2018 through 09-30-2018

Frankly, it makes sense that the market's would behave this way. The international economies that trade with the U.S. have been making boat loads of money on the spread in tariff rates. If this spread goes away, these international economies will lose a major revenue source. But if we truly do get free trade, wouldn't global trade become more efficient for everyone and, therefore, better over the long term?

Time will tell on that one, but on August 17th the USA and Mexico struck a trade deal. Canada followed suit on September 30th.

In July, European Union Commission President Jean-Claude Junker agreed to work with the U.S. to lower industrial tariffs.

And currently, Theresa May and Britain are working with the United States to "rewrite the rules of global commerce." They are trying to draft the "ideal" free-trade deal which aims at eliminating tariffs for nearly all goods traded between the two countries.

Many people hold the opinion that these truly free trade agreements would finally ring in fair global trade and efficient markets for business to operate in. It seems we are living in historic times.

Mid-Term Elections and Beyond

In the last newsletter, it was discussed in "The Grind" article that we expect markets to remain volatile until the November elections are over. Since we didn't see a whole lot of volatility in the 3rd quarter, it makes logical sense that the month of October could show us some gyrations. If this does indeed come to pass, that could set that stage for our entire forecast to come true. Which is, volatile markets before the election followed by market strength to close out the year.

However, there is always a chance our forecasts do not turn out to be completely accurate. In which case, we always seek to analyze alternatives. In this case IF OUR ORIGINAL THOUGHTS DON'T COME TRUE (volatile in October before a year end rally), then it might be the case that the markets remain calm and strong through the election. There is certainly a chance this occurs but it wouldn't make logical sense. Nevertheless, markets are not always rational.

It is our opinion that if the markets do not sell off prior to the elections, then the rally we were expecting off of those lows might not materialize. Why? Essentially, the rally would have already happened. Our thoughts of a big rally to end the year was based off of the idea that the economy is strong and earnings are good but the uncertainty of the elections would put a bit of fear into the market and prompt some weakness. After the elections were over, the uncertainty would be gone and the strong economic fundamentals would be in focus again and the markets would rally.

If the markets never do get fearful of the election, then the rally wouldn't be needed because there was no dip and the strong economic fundamentals would have never left the focus of the markets. Frankly, this is a fine scenario too. As at the end of the day, the market just might end up being in the same place.

Regardless of how the markets end up getting to where they will be by the end of the year, we think two big themes for next year will be inflation and interest rates.

Perhaps the biggest theme in 2018 has been how robust the earnings growth has been for U.S. companies. And in line with this, another big theme is how strong the outperformance of the U.S. market has been relative to the international markets. This is a great story and sets the stage for a fundamentally strong economy.

But the other side of a strong and robust economy within the context of a 10 year expansion is that inflation has to creep in at some point. Especially with historically low unemployment levels and booming earnings.

Inflation at a moderate rate isn't a horrible thing, but if inflation gets out of control it can erode purchasing power and begin to pinch an economic expansion. Historically, central banks fight inflation by hiking rates to slow down economic growth.

And it is these two things that have my full attention at this point. Yes, the economy is booming. Yes, unemployment is low. Yes, earnings are sky high. And all of these things have pushed the market higher. But we need to keep an eye on how high rates go and how strong inflation gets.

Bear in mind, there are investments and sectors that benefit from these two forces. We have been accumulating these types of assets for over 6 months in an effort to prep for these potential occurrences. But, regardless, they might rattle the markets and people who are not prepared.

We will strive to be ready and will seek to take advantage of any irrational market dislocations should these events arise.

In the meantime, if the market gets choppy before the election...that is what we have been planning for all year. We believe our portfolios are positioned to be able to withstand those gyrations. If the market doesn't become fearful of the elections, that is fine too. We will enjoy the profits and continue prepping for potential inflation and interest rate hikes.

Non-Financial Events occurring this quarter

Tiger Woods won the Tour Championship

Naomi Osaka won the U.S. Open

Aretha Franklin passed away on August 16th.

NASA launched a probe to study the sun on August 12th

India ended the crimi-nilization of homosexuality on September 5th

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