

# MRP CAPITAL INVESTMENTS, LLC

## 4th Quarter 2020 Client Newsletter

### Capital Market Update

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As we've been discussing all year, we thought the market would rally after the election regardless of who was elected President. And with the S&P 500 appreciating 11.69% in the 4th quarter, that prediction was indeed correct.

In fact this 4th quarter rally has taken most stock market indices into positive territory for 2020, despite the incredible variance among different indices. And even with the unpredictable nature of 2020, the S&P 500 finished the year with a price change of 16.26%.



S&P 500 2020 Chart Supplied by BigCharts.com



Heading into 2021, there are still some uncertainties regarding how all of moving pieces of the global economy will fit together and we certainly do have a lot to worry about. But Bull Markets are said to “climb a wall of worry.”

The fact that the Fed and the Treasury appear to be working seamlessly together to stabilize and inflate asset prices, gives us a lot of confidence that the direction of the markets should be upward biased for the new year. But, of course, volatility will rear its head throughout the year. Which is why we allocate assets according to everyone's risk tolerance and financial needs.

Happy New Year!

## New Investors

This being the beginning of my 23rd year as a professional investor, I have been banged around by the markets enough to know how they operate. One of the benefits of this is seeing the risks pretty clearly on the horizon. And to be frank, there appears to be some very big risks out there. While at the same time I believe I see clearly what will drive this market higher, despite those risks.

I think the biggest risk in the investment world is centered around how far away from traditional economic principles we have drifted. And I don't mean just the United States when I say "we." I mean the global economy as a whole. As time goes by and economic systems and principles reach their limits and bounds, the world seemingly always comes up with "new" and "revolutionary" economic breakthroughs. I think the Lend-Lease Program from WWII is a good example of a "revolutionary" economic breakthrough.



In fact, one of the most enlightening moments of my investment career came earlier this year while I was performing some fairly intensive economic analysis. It was at this time that I began listening to Stephanie Kelton discuss economics. She was Bernie Sanders' economic advisor during his Presidential campaigns. And she is one of the world's leading experts on Modern Monetary Theory. Of course, MMT is her idea of a revolutionary economic breakthrough. The gist of it is this; if you are the country holding the world's reserve currency, then you can directly print more money rather than issue bonds to make up for budget deficits or spending gaps as your currency is always in demand.



Traditionally trained economists see pretty darn clearly the risks associated with unfettered money printing regarding a nation's currency and the potential economic issues they could face in the future. And, of course, those risks center on inflation, currency debasement, and the potential for a loss of confidence in the currency itself. Obviously, these are pretty serious risks that could cause a loss of faith in a currency and/or a specific economic system.

But as we move more and more towards true MMT, investors keep piling in to the market despite these risks. Why?

I think there are three main reasons why this piling into the market is happening now and, interestingly, seems to routinely happen near the end of Bull Markets.

The first one is simple math. If the world has, say, \$1 billion in total circulation then the prices of the assets that the economic system could support is \$1 billion plus some multiplier for lending that takes place by the banking system with those dollars.

But if the world's governments print an additional \$100 billion, then the prices of assets could go up by a factor of 100. And this is simply because there is 100 times more currency in circulation and, therefore, consumers can spend more money on the things they want.



The second is ignorance. Many market participants are grizzled veterans of the financial markets and they've seen things like this before. However, many investors are younger and new to the markets. They haven't seen this happen before and when they see rising prices, they want to take part in the money making festivities.

And that leads us to the third reason; FOMO. This Fear Of Missing Out is a very powerful force in the markets because markets are made up of people and people are driven by their psychology. When they see prices going up and their peers making money hand over fist, they are compelled to jump in. And this simple action drives prices higher.

In fact, I've written about this rising price action having an impact on the actual fundamentals of a market due to the fact that rising prices of assets/companies gives them more access to cheap capital. This access to capital allows them to implement business ideas with ease, which directly affects markets and pricing. The Theory of Reflexivity is what scholars have called this phenomena.

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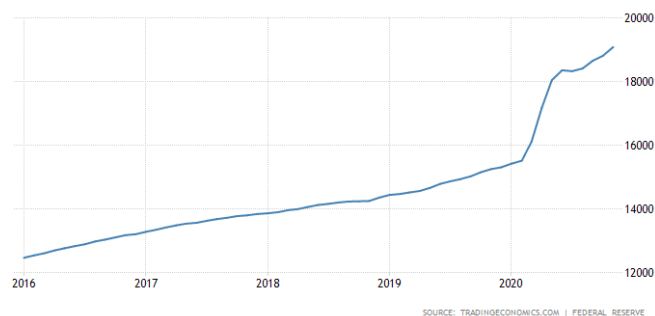
"As you can see, we've not only kept up with the Jones, but surpassed them. Next up, the Nelsons."

What is important to understand is that these concepts usually do drive markets higher. And I do believe we are entering one of these stages. In fact, I detailed the actions taken by the Fed in the last newsletter which helped backstop the economy from the devastating impact of the economic shutdown in response to the Coronavirus. I believe these actions have given investors the confidence to unleash their investment dollars into the market. In fact, take a look at this chart of the money supply and the stock market.

## STOCKS, BONDS & M2



I haven't run a statistical analysis regarding the correlations between money growth and stock market and/or nominal economic growth, but I'm not sure I need to do that. It sure looks to me like when money is printed (the green line) the stock market (blue line) goes up. And we just had a BUNCH of money printing, as this chart from the Fed and Trading Economics of M2 clearly demonstrates.



This concept of new investors entering the market but not really understanding it, isn't a new idea. I'm sure we've all heard the story of a stock market guru getting his shoes shined in 1929, right before the crash, and having the kid shining his shoes give him stock market advice. It is a great story but the true nugget of useful information is that given enough time within a Bull Market, everyone will eventually get invested. And when the last investor has piled his last dollar into the market, there is no more capital to invest and the market can't go higher.



And over the last year, I've seen a few instances of this type of thing happen to me. One example was when I was on a business trip to South Georgia/North Florida. I put on my suit and headed to grab some breakfast before a business meeting. The young man behind the counter who was serving me eggs, asked what kind of business I was in. Of course, I said investments. He proceeded to tell me all about his portfolio and how he had beaten the market for 3 years in a row.



There was another instance that I saw on a social media site of a new Robinhood investor. Evidently, he was trying to make a trade and the Robinhood system wouldn't take the trade. He sent very angry and aggressive direct messages to the Robinhood support staff telling them how unhappy he was that their system was so bad that he couldn't even put a trade on a New York Stock Exchange traded stock and get a timely execution of his order. The response from the Robinhood staff was that, 'the market isn't open on Saturday and he'd have to wait until Monday at 9:30 am EST to get his order filled.'



And finally, I was having an investment discussion with a trader who works for a large hedge fund. We were talking economics and markets and I mentioned 2008 and asked him if he remembered how that awful market flipped into a great market in early 2009 because of some accounting changes made by FASB. His response was that he didn't remember any of that because he was in middle school in 2008.



Obviously, these examples aren't statistical data points that we can use to develop financial or econometric models to help predict future stock price movements. However, they do illustrate that we have new investors that are excited about this market and its money making potential. But they don't fully understand how the markets operate and/or how they've behaved over time. This is a pretty big reason why history repeats itself in the financial markets. And that is, investors can read and study history in an attempt to understand how things have happened over time, but many won't. For those who don't, the only way they will learn is to repeat the mistakes that the older grizzled veterans have already made and learned from. In the meantime, the veterans will be seeking to use their knowledge and their younger counterparts excitement to make money and profit while times are hot, while looking for a good time to take some risk off the table when things get too hot.

On that final point, when will we know that things are getting too hot? Like I mentioned a few paragraphs ago, give people enough time in a Bull Market and they will have all their chips on the table. Add to this the Fed's actions to backstop this market and inflate assets prices and I think we might have an idea of what the final leg of this Bull Market might look like.

President-Elect Biden has said he will name Janet Yellen his Treasury Secretary. Yellen is a former head of the Federal Reserve Board and has said multiple times that the Fed buying stocks could help in a crisis. It just might be worth considering that if the Fed announces they will buy equities, then we might be very near the end of the run up in this Bull Market. Now, for sure, when this announcement is made (if it ever is), the stock market will BOOM! The Fed, supplied with an almost limitless amount of money by the Treasury, would be the major buyer of stocks in the market. And prices will soar!! But after that, who would be left to buy stocks?



In summary, we had a wild 2020. 2021 is looking like it could be just as wild. We have a Central Banking regime that appears to be fixated on rising asset prices to support our debt-based economy. Additionally, we have a new group of excited investors piling into this market. And we have the Fed with an absolute bazooka of an idea to push prices even higher, if it were to decide to buy stocks. With this, we are pretty darn bullish regarding the equity markets at this time.

# The Dollar

As we've previously discussed, the U.S. dollar is the world's primary reserve currency. Most international trades are executed in dollars, many loans are denominated in U.S. dollars (even if the issuer isn't the United States), and most of the global central banks reserves are in US dollars. This fact gives a seemingly unlimited amount of demand for U.S. dollars. And this global demand for dollars allows the United States Congress to consistently spend over and above the amount of revenue they generate from taxes.

Furthermore, in the last newsletter we mentioned that if the dollar were to lose its status of the de facto reserve currency for the world then the demand for U.S. dollars should wane. This decrease in demand could cause some issues for Congress's spending plans. However, there are games the Fed and Treasury can play in regards to this shortfall in demand for the currency. Nevertheless, we think it is important to track the U.S. dollar and other currencies and currency replacements in terms of pricing and demand.



US Dollar Index 2012-2020 chart provided by BigCharts.com

As you can see from this chart of the US Dollar Index, which benchmarks the dollar to a basket of foreign currencies, that the USD is well off its highs but still very strong compared to where it was in the 2012-2014 time frame. A weak dollar historically helps US exporters as their price of goods is cheaper for their customers relative to the goods of their international competitors. So let's just remember that a weak dollar isn't a bad thing in every circumstance.

As we discussed in the last newsletter, most of the world's commodities are priced in US dollars. And after seeing the chart on the last page of the dollar weakening relative to other currencies, you would suspect that commodity prices have been rising. And you'd be correct.



12 month chart of the Bloomberg Commodity Index provided by BigCharts.com

In fact, since the pandemic-related market crash in March/April the Bloomberg Commodities Index is up about 30%.



10 year chart of the Bloomberg Commodity Index provided by BigCharts.com

However, over the last decade commodity prices have significantly fallen. So the cost of commodity based inputs for businesses still are at very attractive prices. Nevertheless, the prices have picked up in the last new months.



Another big topic related to currencies as of late are digital currencies. We are probably all familiar with Bitcoin. And what a wild, wild ride Bitcoin has been (as illustrated below by a chart of the Grayscale Bitcoin Trust (GBTC)).



Chart of Grayscale Bitcoin Trust 01-01-2017 through 12-31-2020 provided by BigCharts.com

With more and more sovereign nations issuing loads of debt and printing fiat currency in unison with that debt, many investors are considering alternatives to our current payment system. It is very possible that digital currencies can help alleviate some investor concerns, but there is also a lot of chatter about government digital currencies.

Long story short, I think the strength of the U.S. dollar needs to be monitored very closely. And, quite frankly, almost every currency in the world needs to be monitored. Any loss of confidence and faith in our current payment system, could cause a lot of problems for the way our economy operates.



And, of course, we will be watching these things as closely as we possibly can as we put our best foot forward to stay abreast of the situation.

## Non-Financial Events occurring this quarter



October 26th, NASA confirms molecular water found on the sunlit side of Mars.



December 3rd, U.N. Commission votes to remove cannabis from the list of dangerous drugs in recognition of its medical value.



The U.S. elections took place in November, but the final results won't be known until after the GA Senate runoff vote January 5th.



Guitar legend, Eddie Van Halen, passed away on October 6th.



October 2nd, Hall of Fame pitcher Bob Gibson passed away. As a sidenote in 1968, he went 22-7 with a 1.12 ERA. His career ERA was 2.91, he struck out 3,117 batters, won an MVP, two World Series', 2 Cy Young awards, and was named to the All-Century team.



Sean Connery, the original James Bond, died on October 31st.

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