PORTAL
ASSET MANAGEMENT

Portal Market Commentary - July 2023

Market Update

July was another month of two tales, as the cryptocurrency and digital assets ("crypto assets") market initially rose +10% in the first half of the month and then fell by -7% to finish the month up +2.5%. This rally was we believe partially due to the long-anticipated SEC v. Ripple case reaching a positive decision: "In the context of secondary market trading on a centralized exchange, the court found that XRP is not a 'contract'."

This finding was viewed as a positive development by industry participants. However, the court also found that the sale of XRP to institutions did constitute an unregistered securities offering. This has created some uncertainty as to the final regulatory outlook, but we expect lawmakers and regulators will react positively to the inevitable mass adoption of this new asset class.

Bitcoin (BTC) lost -3.8% in July as its market dominance fell as per our last newsletter where we stated that; *"we believe that June will mark the top of BTC dominance and the bottom of altcoin under-performance."*

The Portal Digital Fund finished July down -1.7% net of fees and the Radiance Multi-Strategy Fund was up 2.7% vs the market as represented by the CCI30 Index up +2.5% and Bitcoin down -3.8% respectively.

The Destruction of Fiat and Rise of Crypto

We are moving into the third and we expect final phase of this monetary policy experiment of unlimited quantitative easing. This began in earnest in 2008 with bank bailouts that shifted corporate bankruptcy risk to sovereign balance sheets. The debt amped up during the Pandemic lockdowns which required monetary supply (M) to increase dramatically to balance out the drop in the velocity (V) of money caused by 'lock-downs':
Money Supply x Velocity = Price x Quantity of Goods *(*aka GDP)*

The West is now in a "debt trap" and the fundamental macroeconomic principle that will drive global investors to embrace crypto assets is the complete devaluation of fiat that will result in good money replacing worthless money. Unencumbered cryptocurrencies will substantially disrupt highly indebted fiat currencies, supporting our macro view of the eventual demise of debt-laden fiat currencies issued by Central Banks.

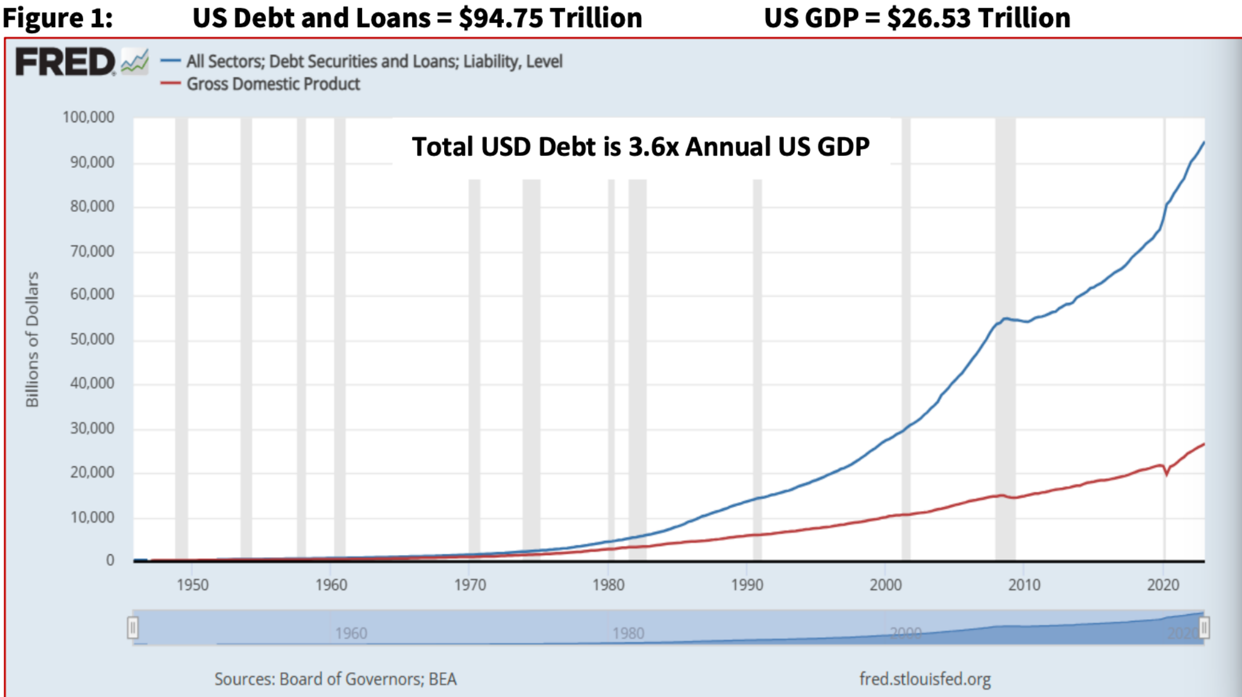
The Debt Super Cycle

As Ray Daglio, Founder and CIO of Bridgewater capital stated: "The 75-year debt supercycle is coming to an end". The structural inflation problem is being driven by monetary inflation – the Fed's ever-growing need to aggressively inflate the money stock and the stock of systemic credit just to maintain government and household liquidity and solvency. i.e., Debt.

The current and expected debt growth as below will eventually stress both borrowers and the balance sheets of creditors. This is the trap: the more indebted a currency becomes; the more additional currency or credit must be created to service and repay that debt.

It is a vicious cycle. Too much money and claims for money is beginning to chase too little economic output, hence the rise in asset prices. As per Figure 1 below, we can see that US dollar-denominated debt is approaching $100 trillion and is growing much faster than the US economy. This equates to "NEGATIVE JAWS", which is essentially a death spiral.

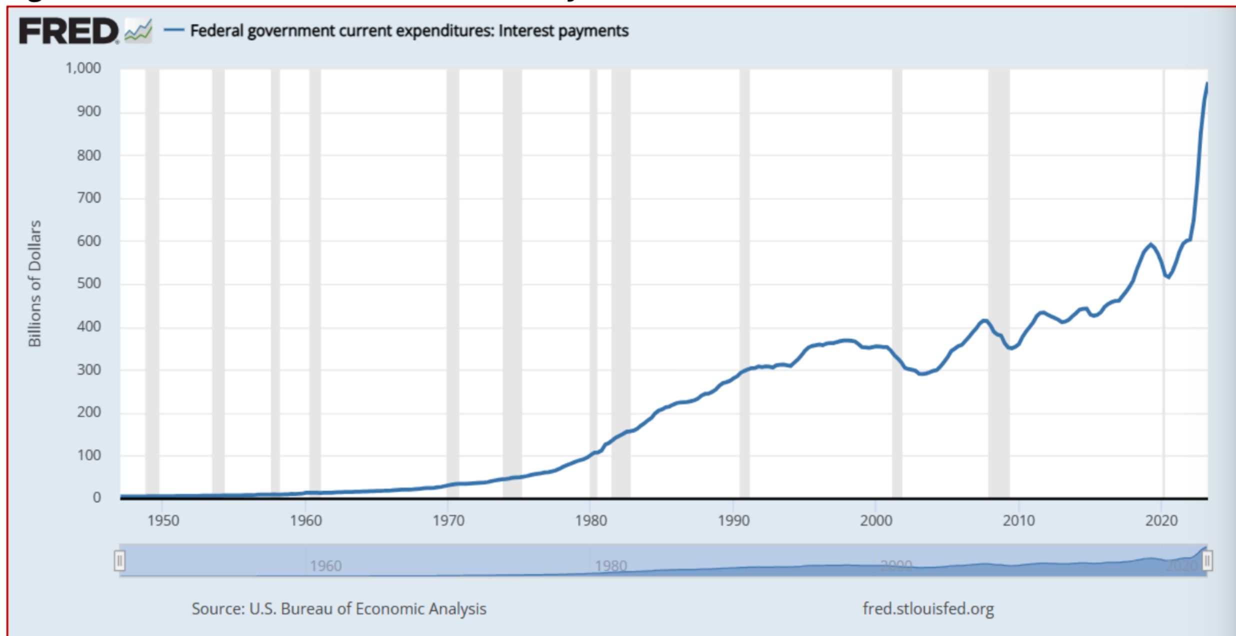
Figure 1: US Debt and Loans = $94.75 Trillion US GDP = $26.53 Trillion



Sources: St. Louis Fed; PostModern Partners.

The result – interest payments alone on money created out of thin air exceeds all tax receipts. This excludes social, infrastructure and defence spending. As per below, the US government's annual interest payments have gone parabolic and is approaching $1 trillion!

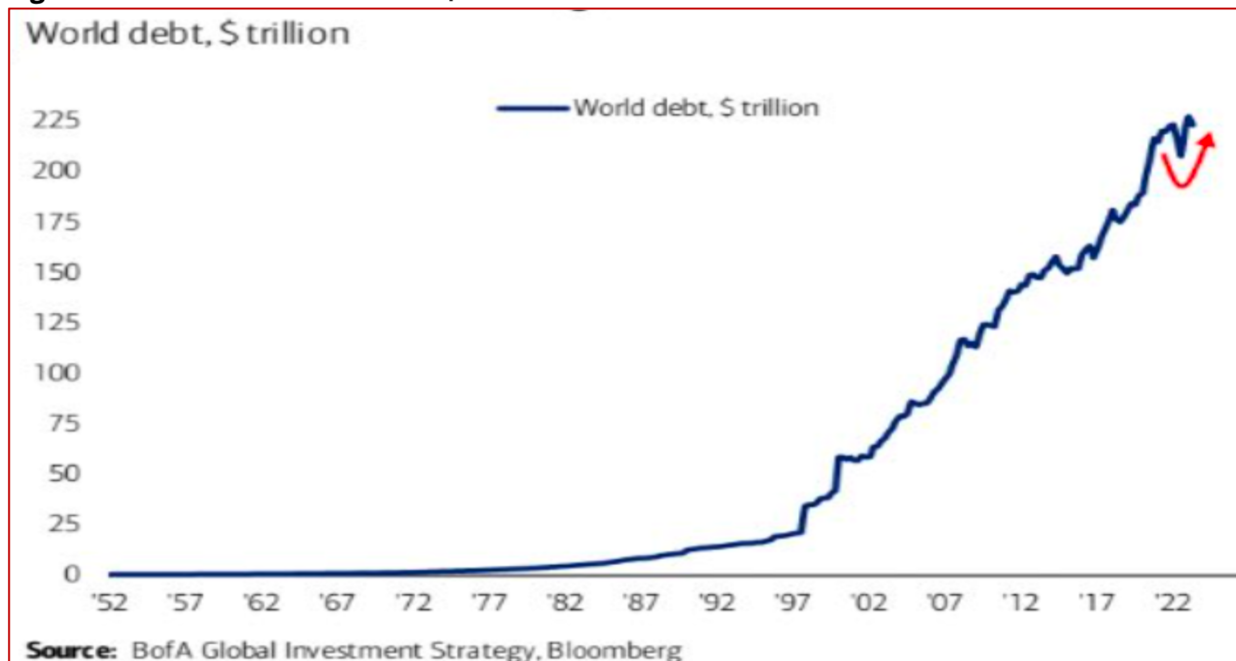
Figure 2: US Government Annual Interest Payments = $970 billion



Sources: St. Louis Fed

Finally, Figure 3 below shows that the massive expansion of debt has been a global phenomenon. The majority of global debt is denominated in **non-dollar currencies** and all the debt is effectively tied to the stability of the dollar, the lynchpin of the global monetary system. When the USD falls, they all fall, including the BRICS.

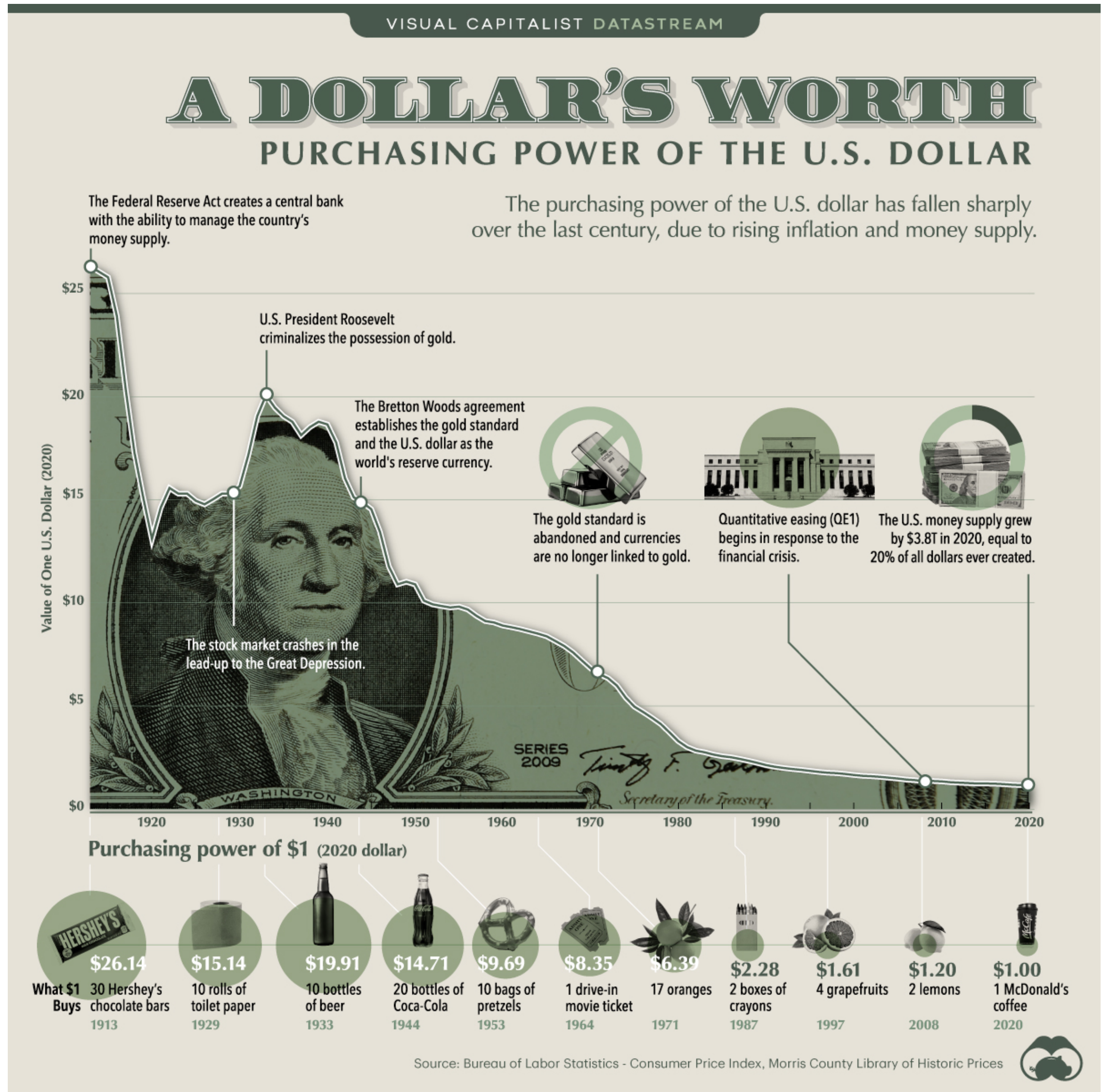
Figure 3: World Debt in Trillions = $225 Trillion



Sources: Bank of America; Bloomberg.

Monetary Inflation Drives Asset Prices Higher

To reiterate, perversely, asset prices are being driven higher today by fiat currency devaluation (i.e., monetary inflation) that's been quietly continuing since 1913 with the creation of the Federal Reserve. This means asset inflation must be high enough to overcome ongoing constant monetary deflation.



This also means annual asset inflation must be higher than annual systemic debt growth, especially when interest rates are above zero. Therefore, the Fed, as the creditor of last resort, has shifted from having the back of the stock market through a "Fed Put" to ensuring asset prices rise – a "Fed Call."

High and rising fiat-denominated debt loads will incentivize younger generations to substitute bad money (encumbered fiat

currencies) for good money (un-levered cryptocurrencies). We should expect ongoing informal fiat devaluations against Bitcoin and other digital and traditional assets including gold, commodities and financial assets with finite stocks.

A central bank digital currency (CBDC) is not a solution to the debt problem because the character of the underlying currency has not changed. The overall debt levels and monetary inflation rates of the dollar, euro, yen, yuan, etc. would remain the same whether or not they exist in banking systems or on blockchain ledgers.

To liquefy their economies, central banks will eventually have to drop rates to zero again and print money to buy assets outright (QE) in far greater magnitude than they had to before. Younger generations will migrate their savings and investment to non-fiat currencies and assets denominated in them.

The Final Masquerade: Fiat Abandonment, Crypto Adoption
We believe the likeliest scenario will be a shift of currencies in which global wealth is denominated and output is driven, from fiat to crypto. It will likely occur gradually, and then suddenly once sovereigns adapt to the digital innovation (e.g., governments will accept tax payments in Bitcoin).

The exchange rates (i.e., crypto prices in fiat terms) of successful cryptocurrencies will rise by many orders of magnitude to levels at which users are relatively indifferent about which currency they hold. At equilibria, exchange rate volatility would be low, similar to USD/JPY today. The fear and loathing surrounding cryptocurrencies will be a memory.

The Investment Case for Crypto
We reiterate that we believe we are at the tipping point of a very rapid surge in adoption of Crypto Assets, and this is underpinned by the actual growth in both institutions and government as detailed in past newsletters, combined with the private sector seeking independent alternatives for everything from money transfers to loans being enabled by DeFi alternatives and the further potential provided in Web3.0.

In addition, cryptocurrencies are unencumbered. Judging by the relative smallness of the crypto market today (1.1 trillion), traditional savers and investors do not seem to care that all prevailing debt is denominated in fiat currencies, and that unencumbered cryptocurrencies will soon be available to replace them.

Impact of a Crypto Allocation on Diversified Investment Portfolios

The crypto market is effectively long-term "VC-like" investing with real-time, public market pricing and liquidity. The biggest positive in allocating to the market is the ability to own liquid assets that can generate returns far superior to those in other markets. The obvious negative is the potential to lose all of one's investment via direct token investment.

The risk of total loss can be mitigated by allocating across various digital asset sectors by use case and time horizons and by limiting one's allocation to the digital asset class to a smaller position, around 2%-5% of a portfolio. This small allocation to the crypto market that could rise by 10x or 20x in the next bull market would likely be a meaningful wealth creator.

Crypto assets are well worth an allocation, especially given their significant upside potential in the form of a perpetual call option on the technology and asset class which we discussed in our previous market commentary's.

Conclusion

We continue to believe that crypto assets are the greatest opportunity for wealth creation and democratisation of access to capital and participation in the global economy and that this will give rise to the next unicorns, regardless of governments attempts to stifle it.

From a regulatory perspective, the safest way for allocating in a compliant and efficient manner to the public crypto market is through a dedicated, regulated, financial service license-compliant cryptocurrency and digital asset focused fund with independent administrators and a fully audited track record that accepts suitable investors only.

Feel free to contact me should you have any enquiries.

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