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Cryptocurrencies and Cheeseburgers

Although there might be a remote (extremely remote) possibility that Bitcoin could someday become the predominant worldwide currency, we feel until there is a likelihood that Joe Schmo could easily use it at the drive-thru to pick up a cheeseburger, its adoption by the common person will be stubbornly slow outside the nerd-world. There is a myriad of obstacles a “cryptocurrency” would have to overcome to become mainstream. For starters, the term “store of value” is often used to describe a basic function of money, and Bitcoin is miserably missing the mark here. How can you rely on making a payment in Bitcoin when its value fluctuates by +/- 10% every day?

What is Bitcoin? Bitcoin is a digital “cryptocurrency” (no paper bills). And it is decentralized, meaning that there is no government or single administrator of this currency.

The good news about Bitcoin is that there is no centralized regulatory body determining how it is issued and distributed. The bad news about Bitcoin is that there is no centralized regulatory body determining how it is issued and distributed.

While cryptocurrency’s future is speculative, there is greater confidence in the many potential practical uses of “blockchain technology” (upon which Bitcoin operates). Blockchain is basically a digital ledger of records that allows for a trustworthy transfer of any digital asset, in this case, Bitcoin. It is infinitely more complicated than that, but our monthly Investment Commentary doesn’t allow for lengthy explanations that make you quit reading.

The reason we even mention it this month is that investor enthusiasm for Bitcoin has gone bonkers recently, reminding us of the tech-stock bubble of 2001. (Can you say “JDS Uniphase”?) As we are writing this on the 7th of December, it is up over 14% TODAY! A year ago, one Bitcoin was worth $757. Two days ago it closed at $11,776. Today, it is over $15,000.

We view Bitcoin’s performance as a speculative frenzy fueled by FOMO (fear of missing out). People are piling in based on the hope they can sell it to someone else in the future at a higher price, and because they are afraid to miss out on becoming an overnight millionaire. The chart below compares Bitcoin in the context of well-known (and other potential) asset bubbles.

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So when you are at a party, feeling incredibly inferior because someone is telling you how their advisor has them invested in Bitcoin and they just bought a yacht, just remember that in 2001 there were braggarts who were crowing about how their advisor had them invested in JDS Uniphase, which was up over 1,000% to around $1,100. In 2008, it traded at $4. Bye Bye, yacht.

And rest assured that Bitcoin will always have one common denominator with all other currencies: Bad people will constantly be trying to figure out ways to take it from you.

Lastly, digital currencies, by definition are completely reliant on a continuously functional internet grid. If that grid is ever significantly disturbed, you will be happy to have paper dollar bills while purchasing your cheeseburger at the drive-thru.

The television media outlets seem to bring us news from Washington in a "rat-a-tat" machine-gun fashion, as if the news is changing every other minute of every day. Donald Trump's election was the best thing that ever happened to media outlets because he is a constant source of new material.

The challenge for us is to sort through the barrage of information and determine which news items are worth our attention.

The vast majority are NOT, but one item that does have our attention is Tax Reform. Both the Senate and the House have passed their (somewhat similar) versions of tax-reform bills and they are in the process of trying to reconcile them.

Although there are many moving parts to the tax-reform bill(s), one of those most talked about is the corporate income tax rate. Currently, the U.S. has the highest corporate income tax rate in the industrialized world. The top federal rate is 35%.

U.S. Corporations have employed different tactics to try to avoid paying this tax. Corporations with international business have frequently chosen to leave their revenues and profits in the foreign countries where they were doing business. This prevents them from "repatriating" those funds to the U.S. and paying the 35% tax. But it also prevents them from investing in newer capital or a larger domestic workforce. Apple alone has over $250 billion in cash overseas — more than the annual GDP of many countries!

A more creative method of avoiding this tax has been to "move" the company's headquarters to another country with a lower tax rate. Ireland has become the site of new headquarters for many U.S. corporations, even when most of the company's business tends to be conducted in the United States.

The proposed bills look to reduce the 35% corporate tax to anywhere from 20% to 25%. A recent rumor has it coming in at 22%. There are other significant changes on the corporate side, such as the rules on expensing and the deductibility of interest, but most Americans want to know, "What does tax reform mean for me?"

This question cannot yet be answered because of major differences between the House and Senate plans. For instance, the House version reduces the number of tax brackets to four and maintains the top individual tax rate of 39.6%, while the Senate version maintains seven tax brackets but decreases the top tax rate to 38.5%. The Senate's plan repeals the ObamaCare mandate while the House's doesn't.

However, we can give an educated guess that the provisions that are the same in both bills will hold up through the reconciliation process, such as the doubling of the standard deduction and repeal of the state and local tax deduction (which affects Californians the most, with a top income tax rate of 13.3%). The estate tax is likely to be much less . . . well . . . taxing. Also, people with large mortgages will lose the ability to deduct interest payments.

Members of the House and Senate are engaging in a conference committee to resolve differences between their plans. We'll have a much better idea about how tax reform will affect different filers after they come out of conference.

Meanwhile, the stock market continues its eight-year bull market, no doubt spurred on by the likelihood of lower corporate taxes. And the bull market may continue for another eight years. Who knows?

Credible reasons that the bull market is not over:

- A painting (which may be fake) sold for $450 million.
- Bitcoin (which may be worthless) soared nearly 700% from $952 to ~$8000.
- The Bank of Japan and European Central Bank bought $2 trillion of [*financial*] assets.
- Global debt rose above $225 trillion to more than 324% of GDP.
- S. corporations sold a record $1.75 trillion of bonds.
- European high-yield bonds traded at a yield under 2%. *[High-yield bonds are considered risky and should trade at a much higher interest rate]*
- Argentina, a serial defaulter, sold 100-year bonds in an oversubscribed offer.
- Illinois, hopelessly insolvent, sold 3.75% bonds to bondholders fighting for allocations.
- Global stock market capitalization skyrocketed by $15 trillion to over $85 trillion and a record 113% of global GDP.
- The market cap of the FANGs [*Facebook, Amazon, Netflix, Google*] increased by more than $1 trillion.
- S&P 500 volatility dropped to 50-year lows and Treasury volatility to 30-year lows. *[Complacency frequently precedes calamity]*
- Money-losing Tesla Inc. sold 5% bonds with no covenants as it burned $4+ billion in cash and produced very few cars.

At Boyer & Corporon Wealth Management we are cognizant of valuations and invest our clients' money in a manner that is consistent with the level of risk they need.