

## Fourth QUARTER – 2021 CLIENT NEWSLETTER

### REVIEW OF THE MARKETS:

Index:	4Q21	2021
<b>S&amp;P 500</b>	11.03%	28.71%
<b>S&amp;P Mid-Cap</b>	8.00%	24.76%
<b>S&amp;P Small Cap</b>	5.64%	26.82%
<b>Morgan Stanley's EAFE (International Stocks)</b>	2.69%	11.26%
<b>Barclay's US Aggregate (Bonds)</b>	0.01%	-1.54%

### ECONOMY & MARKETS:

Heading into the First Quarter of 2022, these are the major headlines affecting the markets:

**Omicron** – This recent Covid variant spooked the market in the last several weeks causing selling across virtually all asset classes. News appears to continue to change on the variant's transmissibility, severity, and ability to evade vaccines. For now, it has caused a lot of volatility in the markets.

**Federal Reserve's recent more aggressive forecast** – In the most recent Fed meeting in December, most Officials released projections that now pencil-in three quarter-percentage point increases in 2022. In the prior meeting in September, The Committee's estimates were to increase interest rates just once. To go from one to three rate hikes is a drastic change. In addition, The Fed approved plans to accelerate the ending of their asset purchase program, now concluding in March instead of June, 2022. Further, the rate of purchases will slow from \$90 billion per month to \$60 billion per month. These asset purchases were intended to stabilize the markets and stimulate the economy. It has been known the Fed wanted to end its asset purchase program before raising rates, dubbed "Operation Liftoff". This now opens the door to interest rate hikes beginning in March, 2022. In our opinion, that is too aggressive and too fast.

**Inflation** – The most recent CPI statistic was reported at 7% year-over-year with core CPI (ex- "food & energy") at 5.5% for the same time frame. Some indicators allude inflation may be peaking though. The rise in inflation has been caused by several factors including supply chain distributions, wage growth increasing due to labor market shortages, oil & gas prices, and others. Traditionally, the Fed uses interest rate increases as a mechanism combat inflation. In our opinion, the FED may not be fully successful in their strategy to significantly curtail higher inflation by raising interest rates. It's a bit unclear as to how raising interest rates will help alleviate supply chain disruptions and clogged ports. However, raising interest rates may still prove to be an effective psychological effect on both businesses and consumers – if interest rates rise, borrowing will become more expensive. This effect may then lead to a reduction in overall spending, which may temper the non-supply chain inflation issues.

**Unemployment** – Since the pandemic started, the unemployment rate has fallen sharply from double digits to 3.9% in December. However, there are still many people that remain out of labor market. With eligible workers staying on sidelines due to the fear of the virus or Baby Boomers retiring early, the actual participation rate is much lower than pre-pandemic making the 3.9% figure above a bit misleading. With job resignations so high in 2021, it was dubbed "The Great Resignation".

<i>Economic Statistics (year-over-year basis)</i>	<i>Most Recent</i>	<i>Previous report</i>
▪ GDP growth rate	3Q21 up 2.3%	2Q21 up 6.7%
▪ Inflation (CPI)	Dec up 7%	Nov up 6.8%
Core CPI (excludes food & energy)	Dec up 5.5%	Nov up 4.9%
▪ Unemployment rate	Dec up 3.9%	Nov up 4.2%
▪ S&P 500 Forward P/E ratio	21.25	Sept P/E was 20.5

*2022 will be YAIA's 15<sup>th</sup> year in business*

*Komal Motwani was recently promoted to Senior Investment Analyst. She has performed a critical role for all of our clients helping analyze client portfolios, meeting participation, and follow-up afterwards. Please feel free to congratulate her at our next meeting!*

*The following pages attached in this newsletter are a client-approved handout published by Schwab titled Cryptocurrencies: What are they?*

*As this topic has arisen a few times by clients, we thought including this would be very timely for everyone.*

# Cryptocurrencies: What Are They?



November 17, 2021

Lately it seems like cryptocurrency is everywhere. From the now-ubiquitous tales of “Bitcoin millionaires” to the increasing number of companies jumping into the crypto arena, it’s hard to ignore the news—or the feeling that not owning cryptocurrency means missing out. The price of one bitcoin has ranged from \$1,000 in early 2017 to more than \$66,000 in October 2021—but with intense volatility, including periodic drawdowns of more than 50%, in between.

So what is cryptocurrency? Should you invest in it? How can you invest in it? We’ll cover all three topics in this and related articles. For now, here are answers to some of the most common questions about the basics of Bitcoin and other cryptocurrencies.

## What is Bitcoin?

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Bitcoin is a virtual, digital, or “crypto” currency—so called because of the cryptography, or unchangeable coding techniques, involved in the blockchain code on which they exist. The intent of Bitcoin is to allow online payments to be made directly from one party to another through a worldwide payment system, without the need for a central third-party intermediary like a bank. Bitcoin is not issued by any central bank or government and is not legal tender (meaning a national currency established by statute) in any country except El Salvador. Like physical gold, Bitcoin’s value stems from a combination of scarcity and the perception that it is a store of value, an anonymous means of payment, or a hedge against inflation.

## What’s the relationship between Bitcoin and blockchain?

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Blockchain, the underlying technology that supports cryptocurrencies, is an open-source, public record-keeping system operating on a decentralized computer network that records transactions between parties in a verifiable and permanent way. Blockchain provides accountability, as the records are intended to be immutable, which presents potential applications for many businesses. While blockchain has often been associated with cryptocurrencies, it has many potential uses beyond payments, including smart contracts, supply chain management, and financial services. Note that ownership of Bitcoin or other cryptocurrencies is not an investment in blockchain, the technology, or its current or future uses.

## What is cryptocurrency, and how is it valued?

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Fiat currencies like U.S. dollars and euros are forms of money issued by governments to serve as legal tender. Cryptocurrencies such as Bitcoin, on the other hand, are “non-fiat,” non-governmental forms of “digital cash” to be used for electronic payments. The idea of “digital cash” isn’t new—it started with credit cards, PayPal, Venmo and other services’ need for easy, traceable electronic payments. But those payments are tied to fiat currencies managed by central banks, whereas cryptocurrencies are managed by technology, specifically cryptology. Proponents believe the value of a cryptocurrency is based on the quality of the cryptology, the number of cryptocurrency units created, and the technology that limits the creation of additional units. Like any traded item—think baseball cards—the value depends on supply and demand: The fewer units available, the higher the price buyers are willing to pay.

## **Why has Bitcoin become popular?**

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Like many new technologies or products, Bitcoin attracted adherents interested in innovation and the perceived absence of governmental control. Traders saw it as an alternative to traditional investments such as stocks, bonds, and cash, and trading momentum led to a rising, if highly volatile, price. All of this attracted media attention, which drove mainstream awareness and ultimately, increasing acceptance, and a market to trade it. Most recently, companies including PayPal have announced that they’ll support or accept Bitcoin as a form of payment.<sup>1</sup>

## **Who oversees Bitcoin?**

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Bitcoin was created based on a paper written in 2008 by a “founder” who goes by the pseudonym Satoshi Nakamoto, but no person or agency currently regulates it to ensure that it maintains value and liquidity and works as a means of payment. It’s governed by consensus of a private digital community according to guidelines based on the community, cryptology, and a network of computers. While individual countries may allow Bitcoin to be used as a means of payment, regulate the terms under which its citizens can trade or mine Bitcoin, and authorize the operation of cryptocurrency exchanges, they don’t regulate/control the existence or value of Bitcoin itself, or the blockchain code on which it operates. Bitcoin is promoted by the Bitcoin Foundation, but the foundation also does not control or manage Bitcoin’s trading or value. The number of bitcoins in circulation is limited by and managed by computer code and traded through one of several digital, decentralized exchanges.

## **How many investors own Bitcoin?**

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No one knows for sure, but according to Bloomberg, as of November 2020, 95% of all Bitcoin was held by only 2% of all account holders.

## **Is Bitcoin the only cryptocurrency?**

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No. Bitcoin was the first cryptocurrency and it is the best known, most widely held, and—with about 44% of the total cryptocurrency market cap<sup>2</sup>—the most valuable. However, as of October 2021 there were thousands of digital currencies in the marketplace, of which more than 100 have a market capitalization exceeding \$1 billion. Some of the more popular cryptocurrencies include Bitcoin Cash, Cardano, Tether, Ethereum, Polkadot, and XRP.

In October 2021 Federal Reserve Chair Jerome Powell and SEC Chair Gary Gensler both stated that they didn’t intend to outlaw cryptocurrencies, but Gensler said the SEC was exploring how best to ensure that the industry protects investors and consumers and follows anti-money laundering and tax compliance laws.

China already has launched a digital yuan and it is estimated that at least 80 different countries around the world, including the United States, are exploring the idea of launching their own proprietary Central Bank Digital Currency. While the Fed, the U.S. Treasury and the SEC have been noncommittal on the topic, in October 2021 Powell remarked that “it is more important to do this right than to do it fast.” This implies that it may not be a matter of “if” but rather “when” the U.S. develops its own digital dollar.

## Bottom line

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Schwab continues to monitor cryptocurrencies as regulations and technology evolve. While some traders have made money on the change in price of Bitcoin or other cryptocurrencies (and others have lost money), we suggest that most investors treat them as a speculative asset primarily for trading with money outside a traditional long-term portfolio.

<sup>1</sup> Molina, B., “PayPal to let users pay for purchases at checkout using Bitcoin, other cryptocurrency,” March 30, 2021, *USA Today*.

<sup>2</sup> According to October 3, 2021 data from [coinmarketcap.com](https://coinmarketcap.com), indicating Bitcoin market cap of \$1.2 trillion, and total global crypto market cap of \$2.73 trillion.

### About the author

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**Past performance is no guarantee of future results and the opinions presented cannot be viewed as an indicator of future performance.**

**Investing involves risk, including risk of loss.**

Digital currencies, such as Bitcoin, are highly volatile and not backed by any central bank or government. Digital currencies lack many of the regulations and consumer protections that legal-tender currencies and regulated securities have. Due to the high level of risk, investors should view Bitcoin as a purely speculative instrument.

Currencies are speculative, very volatile, and not suitable for all investors.

Futures trading involves a high level of risk and is not suitable for all investors.

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