

MARKET COMMENTARY – OCTOBER 1, 2017

What the heck is a Bitcoin?

Bitcoin, Ethereum, and Litecoin are just three examples of so-called *blockchain* or *cryptocurrencies*. There may be as many as 700 others in existence today! But what the heck are they, really? And if we can even accurately define them, are they or their ilk something that clients ought to own?

First, what is a Bitcoin? As you've likely suspected, it is not a coin at all. There are no governments printing or stamping Bitcoins and then proclaiming them legal tender. In fact, there is nothing physical to look at, pick up, or feel. And there never will be.

But wait, you may say, I've heard there are people called Bitcoin miners. They're mining for something. Well, yes. But we must start at the beginning.

Consider a blockchain, an encrypted digital ledger of assets and transactions that is NOT stored on one central computer. It is hosted by millions of computers simultaneously. As such, while the data is accessible, it may be considered safe since it is not controlled by a single entity like a bank and therefore has no single point of failure (as during a hack). In theory, to truly hack these cryptocurrencies would require a vast amount of computing power because the data is so far distributed.

Let's say there are two individuals who agree to settle a transaction using Bitcoins instead of dollars. One is buying a car from the other for 10 Bitcoins. The two send the terms of the agreement over the distributed network.

Others, who have decided to voluntarily join the network as miners, begin crunching all the encrypted data using computers. Each transaction becomes a race to complete and record by these miners. The miner that successfully ties together all the data in the transaction between the two parties effectively seals it off so that no one may tamper with it any longer. That completed information is called a *block* and is added to the long *chain* of existing data. The first miner to do so is awarded a specified amount of Bitcoins for the trouble.

We may picture cryptocurrencies, kind-of, if we think that Bitcoins have their value backed by all the mathematical and computing power that goes into creating each new coin. The value of a cryptocurrency is not set by governments, but by individuals in competition using powerful hardware and dizzyingly complex software.

OK. But is it real? Will it last? Is it a fad, or worse? It depends on who you ask.

Jamie Dimon, the CEO of JP Morgan, has said that cryptocurrencies are *stupid*. He added that they might be appropriate to use if you are in Venezuela, North Korea, or are a murderer. Harsh criticism indeed. But he was careful to separate the concept of Bitcoins from the underlying blockchain technology which can be useful for all sorts of things that involve recordkeeping.

The Wall Street Journal recently ran an opinion piece that stated there is *no chance whatsoever that bitcoin can displace the dollar, for the simple reason that it is badly designed*. The article went on to list several technical problems that are specific to Bitcoin and not the 699 other potential competitors or any new rivals yet to spring into existence.

China recently declared all cryptocurrencies illegal.

On the other hand, there are cryptocurrency cheerleaders. Most of them are folks you've never heard of, geeky tech evangelists or miners trying to get rich. A lot of them come from non-Western countries with a history of being unable to trust banks or governments. The miners are mostly anonymous individuals or pools using monstrous networks of computers to process transactions. But there are a few respectable pioneers who believe that Bitcoin matters, among them Marc Andreesson and Tim Draper.

So, should we invest in Bitcoin? In any of the cryptocurrencies?

We say, NO, not now. Not directly. There are too many similarities to the hype surrounding specific cryptocurrencies that resemble manias, bubbles, or pyramid schemes. BUT, we do not deny that the concept of a distributed network of computers working on the blockchain to verify transactions is an idea that has value and will likely become at least a part of the backdrop of financial transactions, file storage, auditing, data management, identity management, et cetera. Therefore, we won't purchase any Bitcoin. But we will continue to invest in the technology and systems that facilitate its use.

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Sincerely

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