



OUR MISSION IS TO CHANGE LIVES. **ONE "HEMINGTON" AT A TIME.**

# HEMINGTON NEWSLETTER

SPRING 2022

## Understanding the Cryptic in Cryptocurrencies

By Amy Mitchell, CFA, CFP®, and Eileen O'Connor, MBA, CFP®



**The prefix crypto- is derived from an ancient Greek word meaning "I conceal" or hidden or secret. This is an appropriate starting point for a discussion of cryptocurrencies. Since the first one, Bitcoin, was mined in 2009, there remains much misunderstanding of what cryptocurrencies are and what role, if any, they could play in a portfolio.**

Many people who buy cryptocurrencies do so for a chance to strike it big and avoid FOMO, or the "fear of missing out." By far the largest cryptocurrency, Bitcoin has seen its price go from \$0 in 2010 to about \$28,000 as of this writing – for no rational reason other than increased demand from investors. The price peaked at \$65,000 in April 2021 – and then dropped by 50% in the span of three weeks. There are thousands of cryptocurrencies in addition to Bitcoin which have dominated the news in recent months, prompting many questions. Below we give a high-level overview of cryptocurrencies as an asset class and provide Hemington's current perspective on the opportunity.

### WHAT ARE CRYPTOCURRENCIES?

Unlike traditional money, cryptocurrencies do not involve paper notes or metal coins. No central bank issues the currency, and no regulator or nation state stands behind it. A recent Financial Times article defined cryptocurrencies as "assets that have been created digitally by a private company to serve as a store of value, which can be used to exchange for goods and services." Said another way, cryptocurrencies are a form of code made by computers and stored in a digital wallet.

Its value is transferred and recorded on open "peer-to-peer" ledgers known as blockchain. The currency's provenance and transfer of ownership is secured and verified by cryptography, an encryption process.

This decentralized, peer-to-peer approach to transactions takes place through the use of blockchains. Bitcoin is created as a reward for "miners" who use computers to solve puzzles and verify transactions that are made on the Bitcoin blockchain. In a blockchain, timestamps for a transaction are added to the end of the previous timestamp, creating a record that cannot be changed. Blockchain records are kept secure because the amount of computational power required to reverse them discourages attacks. The process is expensive and requires high energy consumption.

### HOW AND WHY WERE CRYPTOCURRENCIES CREATED?

Satoshi Nakamoto is the illusive figure purported to be Bitcoin's creator, though the identity of the person (or group) has not been uncovered. Bitcoin's central idea was to allow anyone in the world to open a digital bank account or wallet and hold the money in a way that no government could prevent or regulate. Bitcoin is governed by a network of computers using the same software (with the Bitcoin rules), and the software includes a complex algorithm that makes it possible to create an address and related private key known only by the person who created the wallet. The software allows Bitcoin network to confirm the accuracy of the password to allow transactions but without seeing the password itself. No identity check is required. No more than 21 million Bitcoin will be mined.

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## WHAT HAPPENS IF YOU LOSE YOUR BITCOIN PASSWORD?

Bitcoin exists only as computer code and is generally kept in a “digital wallet” accessible by a (very long) password chosen by the user. If the password is lost, there is no way for the holder of Bitcoin to retrieve it. The New York Times reported that a man has a digital wallet of 7,002 Bitcoin he acquired in 2011 and is now worth over \$200 million – but he lost the paper on which he wrote the password and has only two remaining attempts before he will be locked out. Apparently, his case is not unusual. An estimated 20% of all outstanding bitcoin are stranded assets that their rightful owners can no longer access.

## WHAT ARE THE RISKS WITH OWNING CRYPTOCURRENCIES?

Beyond the possibility of losing your password, there are significant risks with owning cryptocurrencies.

- » **Extreme volatility.** Most prices of cryptocurrencies are very volatile. Some cryptocurrency owners follow the mantra of “HODL,” or hold on for dear life!
- » **Not backed by an issuing authority.** Cryptocurrencies are mostly unregulated. If anything goes wrong, owners have little protection by authorities.
- » **Delisting.** Cryptocurrencies can be delisted or discontinued for many reasons, including low volume, low liquidity, and security breaches. There is no recourse if a cryptocurrency is delisted.
- » **Security risks.** The owner of cryptocurrencies is responsible for safeguarding the asset. A digital wallet can be kept online and allows for easier owner access – but that also makes it easier for hackers to access. Another method for holding cryptocurrencies is in “cold storage,” an online electronic device in a vault not connected to the internet. This method is more secure but also more expensive and does not accept as many kinds of cryptocurrencies as online wallets. Of course, owners are responsible for safeguarding the password.
- » **Political uncertainty.** The White House has ordered a broad review of the possible risks cryptocurrencies may pose to the stability of the financial system. It also plans to study the creation of a U.S. digital currency that would be issued by and backed by the Federal Reserve—potentially making unregulated cryptocurrencies less desirable.
- » **Uncertainty with the technology.** There are questions around whether the underlying technology will be adopted further in the future—and if so, how? It’s possible that the blockchain technology will be used in different ways with other products, rather than cryptocurrencies.

## SHOULD YOU HOLD BITCOIN IN YOUR PORTFOLIO?

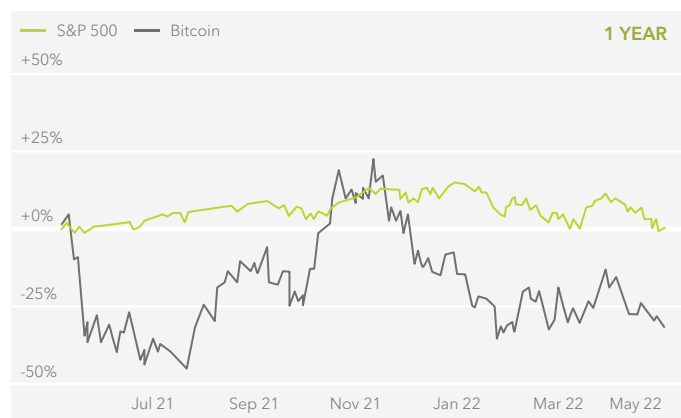
As a thoughtful, long-term investor, it is important to employ an investment strategy that is evidence-based and has a successful track record. In well-structured portfolios, we seek the following objectives:

- » **Positive expected returns (stocks and bonds).** With Bitcoin, there is no expected cash flow and no positive expected returns. The owner of a Bitcoin is hoping that someone else will buy the Bitcoin at a higher price in the future.
- » **Mitigation of risk/uncertainty (government bonds and inflation protected bonds).** Bitcoin is extremely volatile, which would increase portfolio volatility without an expected return.
- » **Liquidity for short-term expenses (cash).** Liquid assets need to hold their value to ensure that you can pay for expenses when needed. Bitcoin and other cryptocurrencies can fluctuate in value by 10-20% or more in any one day, making it nearly impossible to price goods and services in Bitcoin.

At Hemington, we are not including cryptocurrencies in client portfolios at this time. For clients who want to own cryptocurrencies, we recommend that you should not own more than you can afford to lose and preferably less than 1% of your investable assets. Please reach out to your wealth advisor if you have questions or would like to discuss further.

## BITCOIN VS S&P 500 OVER THE PAST YEAR

Performance from May 4, 2021, to May 4, 2022



Over the past year, Bitcoin has dropped almost 32%, while the S&P has been relatively flat with a return of 0.19%.

Source: Coinbase



# WHAT'S NEW AT HEMINGTON?



A recent **Yahoo Money** article featured **Eileen O' Connor** sharing her concerns on the new option of investing in cryptocurrency in 401(k)s now that Fidelity is going to allow retirement plans to offer Bitcoin as an investment choice for participants' accounts.



**Eileen O'Connor** & Hemington Wealth Management were honored on the **Washingtonian** magazine **List of DC's Top Financial Advisers for 2022**. For the eighth time, Eileen O'Connor was recognized on this annual list of the best financial advisers in the Washington, DC area. Washingtonian magazine compiled the list by surveying hundreds of regional financial professionals and asking them: **Whom, besides yourself and your business partners, would you trust with your own money?** Those survey results, coupled with Washingtonian's independent industry research, formed this 2022 list where the "best adviser" names mentioned are the professionals who received the strongest recommendations.



**Jen Dawson** was featured in this month's **National Association of Personal Financial Advisors** magazine with her article, **"Help women avoid the burden of the 'mental load' at your firm."** In it, she "challenges organizations and women leaders to notice and consider a few areas where women tend to spend a disproportionate amount of time and mental energy at work" so that everyone can benefit from a more fulfilled professional balance.



**Eileen O'Connor** was delighted to return to her alma mater, **The University of Virginia's McIntire School of Commerce**, as a guest lecturer. She shared her journey from student to business owner for fourth year Entrepreneur majors.



## Hemington is Growing!

**Ben Corson, CFA, CRPC**, joins our team as Head of Trading where he oversees the daily portfolio trading operations. He ensures proper client portfolio asset allocation and works with Wealth Advisors to implement portfolio changes in the most tax-advantaged manner. Ben also leads Hemington's Investment Committee.

Prior to joining Hemington, Ben was a Partner at an investment management company. He graduated from American University with a Bachelor's Degree in Business Administration, with a specialization in Finance and a minor in Mathematics. Ben is a CFA® charterholder, a member of the CFA Society of Washington, and holds the Chartered Retirement Planning Counselor (CRPC) designation. He lives in Washington, DC, with his fiancé Ali, where they enjoy trying new recipes and restaurants. He also likes to play and watch sports, especially baseball and golf.

In March 2018, HBO's John Oliver said of cryptocurrency:

**"Everything you don't understand about money combined with everything you don't understand about computers."  
Not much has changed in four years.**

## Need to share a document electronically with your Hemington team?

Be sure to use one of our secure upload links! A secure upload link may be found in each Hemington team member's email signature. When you upload a document, the document is accessible only by that team member until it is stored in your client folder.







# WHAT'S NEW AT HEMINGTON?



Above: Some of the Hemington team met in Chicago for team building. The group took a boat tour, played pickleball, and enjoyed a good meal and each other's company.

Top Right: Appreciating a beautiful spring day in Virginia at Happy Hour.

Bottom Right: Hemington team members enjoying a business lunch out of the office.



## About Hemington Wealth Management

Hemington Wealth Management provides high net worth individuals and families with a broad range of wealth management services including portfolio management. We are collaborative, accessible and responsive, making it easy for clients to work with our team.

## Hemington Wealth Management

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