Spring 2021

"Doh!" For Dough?

In January 2018, Peter Kell found himself in a bidding war at an auction that would alter the landscape of alternative investing. "After we get past the $10,000 range," Kell told *Know Your Meme*, "the crowd just freaks out every time somebody says something." After Kell's $39,000 bid, the auctioneer counted down and declared the item sold. But a problem arose when Kell reached the stage and found the other bidder standing there, believing he'd won. The crowd noise was so deafening, neither could hear the other's bid.

A coin-flip would decide the winner. The tension piqued, Kell won.

For his trouble and cash? A non-fungible token (NFT) of Homer Pepe (a morph between the Simpson's character and Pepe the Frog, a cartoon character that inspired myriad internet memes). It's a digital token, so not tangible, like a painting or baseball cards. In fact, you could take a moment now to hop online and copy and paste the Homer Pepe image. But NFTs are entered into a blockchain, such as Bitcoin or Ethereum, decentralized and unchangeable registries of digital transactions. So, when the coin-flip went his way, Kell became the *owner* of the Homer Pepe. And the image you may have copied and pasted is the same as every Mona Lisa outside the Louvre – a replica.

If you're unfamiliar with NFTs, you might be scoffing—after all, the value of this investment, unlike stocks, isn't based on any real-world events. And you wouldn't be alone. "I got laughed at for a long time after this purchase," said Kell, "but in my head, I was like, 'I can't be the only one in the world to want this.'" He was proven right last month, when his Homer Pepe was sold for $312,000.

For a service charge and "gas fee" (fuel used to process), you, too, can create an NFT. Jack Dorsey famously sold his first tweet, easily found on the internet, as an NFT for close to, brace yourself, $3 million. And an NFT doesn't have to be a visual. A Brooklyn filmmaker sold a 52-minutes audio recording of farts, amassed during the COVID lockdown, for $85.

We'll give you a minute to collect yourself.

Like many investments, NFTs are purchased because buyers believe someone will eventually pay more for them than they did. Unlike most investments, it relies heavily on sentiment, and takes speculation to new heights.

Which breeds excitement and fear, and may be the reason we're getting so many questions about NFTs, as well as other alternative assets like crypto and SPACs. You've likely heard of the former—a unique digital algorithm, logged and verified on blockchain, that can be bought, sold, or traded quickly and safely. You might not know, however, there's an emerging belief that it could become the new gold. Cryptos are untethered from government actions and policies, which, to some minds, make them an ideal hedge against uncertainty (gold's long-time and current role). Given the scads of money governments have spent on pandemic relief, running massive deficit spending, there's certainly an appeal to a currency that can't be printed with reckless abandon. But the world of crypto is mostly unregulated and anonymous, making it an ideal way to fund nefarious activities.

SPACs (special-purpose acquisition companies) are companies with no existing business operations. They are generally formed by investors with an expertise in a specific industry to raise money, through an IPO, to buy an existing company. What makes investing in the IPO risky is the company doesn't identify the targeted acquisition. It's a leap of faith, which is why SPACs are often referred to as "blank check companies." Most individual investors aren't equipped to identify and choose the crackerjack management team behind the SPACs. Adding to the risk, liability insurance rates for SPACs are skyrocketing – coverage to indemnify a SPAC's directors and officers has grown to more than $1 million, up from about a quarter of that over the last few years. Under various names, SPACs have been around a long time, but have come back in vogue—about 300 have launched this last quarter alone, raising almost $100 billion, more than all of last year.

There are many reasons alternative asset classes have taken off. One of those, to our mind, is the hit bond markets are taking. Central bank stimuli have pushed interest rates to extreme lows and bond prices up; consequently, cash yields aren't close to what they were just a few short years ago. In response, many investors have looked to other sources of return – by adding more equity, lengthening maturities they're willing to hold (unwise, in our estimation), or adding to slightly more risky high yield, lower-quality bonds. And, of course, SPACS, cryptocurrencies, and NFTs.

While these alternative asset classes are here to stay, their popularity is likely to wane as the attractiveness of traditional assets – in this case, bonds – returns to normal. With vaccines steadily rolling out, much of the world's populous easing back into everyday life, and huge government spending, growth in the near future could be the best in postwar history.

While these high-risk opportunities aren't a focus of our investment strategies, we constantly keep a close eye on them and their evolutions. Meanwhile, we'll keep employing the time-tested methods we've always used for you and your investments.