KEMP Financial Management, LLC

April 2021: Back to the Future

KFM Update

The Covid-19 vaccines continue to make their way into the arms of many in Southern California. We hope the same is true for you and your community. It is great to see businesses beginning the process of reopening. All of us at KFM have also noticed an uptick in traffic on the road. Vaccines, smiling business owners and traffic all seem be signs that we are finally moving forward.

With the reopening of Orange County along with the recognition that we have plenty of space in our office to be socially distant, we do feel that we can begin to move forward with accommodating face-to-face meetings effective immediately. We will be spacing out our in-office visits to accommodate sufficient time to follow the CDC guidelines in between meetings. For all in-office visits, a Self-Declaration form will need to be completed in advance of your in-office meeting. This can be completed online and/or in the office prior to your meeting.

Your safety and comfort is our number one priority collectively with the safety of our Team. Virtual meetings will always be available should you prefer. Our virtual experience continues to be an area of focus as we ultimately want to have the same experience as if you were physically in our office.

Your Team continues to work on improving our online presence and experience with adjustments and fine tuning of our Client Portal. We are working towards “chatting” functionality through the Client Portal along with enhancing our “virtual” experience outside of GoToMeeting. The kinks on both platforms are still being adjusted, but we hope to have enhancements to both by the end of the second quarter 2021. If you would like to have access to the KFM “app”, available for Android and Apple, please contact our offices at your earliest convenience.

KFM has most recently touched $200m under advisement. While this may not be important to you, for us it is a significant milestone. We would not be at that level without the recognition of the continued trust and confidence placed in our firm and our Team by you. We have been on this journey with many of you for more than twenty years. However long you have been with KFM, we greatly look forward to the journey that lies ahead over the next twenty years and beyond. We are grateful for each of you and grateful that we get to be on this journey together for many years to come.

Capital Markets Update

2021 is off to another great start with the capital markets advancing nicely. If we look at the past 14 months coming off the March 2020 lows, candidly the returns are beyond amazing. We believe you will be pleasantly surprised by the year-to-date results and hope you enjoy the review of your quarterly statement.

Our update meetings this quarter have included an educational piece that has updated data from the research presented in our book (pages 73-78). If you have been listening to the financial media over the past 6 months (which we discourage) you may be hearing the word “rotation”. While US Large Company Stocks have dominated asset class performance over the last 10 years, US Large Value and US Small Stocks are beginning to gain more attention from investors these days. The press has named this “rotation”. You can see this “rotation” beginning in the fourth quarter of 2020 and continuing through the first quarter this year. We will share more information about this “rotation” during your upcoming update meetings. We promise to keep it brief :)

Legislative Update

Taxes . . . another consistent topic of conversation these days following the election. As speculation fills the airwaves on the new “infrastructure plan” which follows the recent “rescue plan,” the discussion by the current administration includes potential increases in taxes. As of this writing, NOTHING has changed and there is no reason to panic or react to the tax news of the day. However, the topics which we think are of interest or certainly topics for future planning for our clients include:

- Potential increase in the Corporate Tax Rate
- Potential decrease in the estate tax exemption (2021 is set at $11.7m per person)
- Potential increase in estate tax rates
- Potential elimination of the Step-Up in basis rules for assets that are inherited
- Potential increase in the Capital Gains Tax Rate for top income tax bracket (2021 top income tax bracket for Single / Head of Household $523k income or more / Married Filing Joint $628k income or more)

Our purpose of calling these out now is simply to let you know we are paying attention. As the year continues to progress, should there be any reason to take meaningful action based upon the future tax landscape, your current and future update meetings will be a great venue to discuss the potential impact on your personal situation. While these are simply “headlines,” if they become real we will have more to discuss as issues become clearer as they relate to your situation.

At Kemp Financial Management, we have always maintained the phrase: “Never let the tax tail wag the dog.” As an example: Should you sell all of your assets based upon what we think may happen? Absolutely not. We’ve been doing this financial advisory “thing” for over 34 years. The estate tax exemption amount used to be $600,000 per person in 1987 (Source taxfoundation.org) today its $11.7m per person. The maximum tax rate for income earners above $108.000 was 70% in 1980 (Source taxbrackets.org) today the top rate is 37%. What we do know is things change. As they change, perhaps fine tuning of your long-term plan may be in order. Please expect ongoing dialogue about these important issues going forward.

Back to the Future (For your entertainment should you have the time)

Back in the late 90s there were some funny advertisements about how you can invest on your own, retire at 25 and own your very own personal island. It got to a point that everywhere you went, people were literally only talking about their personal successful stock trades, with technology “internet” stocks being the stock of the day. So much so was this talk, that when I traveled by plane, I found it best to tell the people sitting next to me that I was clergy, or better yet, a life insurance sales person. This was a guarantee for a quiet flight.

Here are some of the high flyers that I remember: eToys.com (on-line toy retailer), Flooz.com (an alternative to credit cards), Webvan.com (grocery delivery), theGlobe.com (create your own website), Worldcom (global communications), JDS Uniphase (optical communications) just to name a few.

Fast forward to 2021 and it’s beginning to sound the same way. Casual conversations in “safe, social settings” are quickly turning to get rich quick conversations. While the 90s presented arguments about why you should own the high flyer stocks, today’s conversations are built more upon products people, including myself, really do not understand. To me, the discussions today are more like buying a lottery ticket in hope to be really, really rich. To me, it’s a fad that is candidly scary. It’s called greed and we know greed is not an investment strategy.

So here’s what it’s like to be a financial advisor today:

Question: *So tell me what do you do*?

Answer: We currently manage approximately $200m for 150 families. Their primary objective is to maintain their current standard of living without running out of money over their lifetimes.

Response/Question: *That's interesting . . . so how much of the $200m do you invest in Cryptocurrency, SPACs, and NFTs? Did you own Game Stop?*

When I answer zero or none to all of the aforementioned questions, I get an earful at how stupid I must be for not recommending Cryptocurrency, SPACs, NFTs or Game Stop to my clients. That is the similarity between then (2000-2002) and now (2021) and it is called greed. Invest in anything and the outcome will be beyond your wildest dreams. Last I checked the outcome in 2000-2002 was a technology bust that caused over 450 publicly traded companies to disappear quite frankly almost overnight.

So you can engage in lively conversations with your friends or family, here's a brief overview for your entertainment.

Cryptocurrency, specifically Bitcoin: "Everything you don't understand about money combined with everything you don't understand about computers."—HBO's Last Week Tonight with John Oliver, March 11, 2018. It's a great quote. I have spent the last couple of years trying to understand it and I personally and professionally admit, I do not. On the one hand, you have Warren Buffet who believes cryptocurrency holds no intrinsic value while Elon Musk through his corporation, Tesla, purchased hundreds of millions of Bitcoin giving some people motivation to buy it as well. So, who is right, Warren or Elon?

Bitcoin is not backed by an issuing authority and exists only as computer code, generally kept in a so-called "digital wallet," accessible through a password chosen by the user. Many of us have forgotten or misplaced computer passwords from time to time and have had to contact the sponsor to restore access. No such avenue is available to holders of Bitcoin. After a limited number of password attempts, a user can permanently lose access. Since there is no central authority responsible for Bitcoin, there is no recourse for the forgetful owner: a recent New York Times article profiled the holder of more than $200 million worth of Bitcoin that he can't retrieve. His anguish is apparently not unusual—a prominent cryptocurrency consulting firm estimates that 20% of all outstanding bitcoin represents stranded assets unavailable to their rightful owners.

I admit that I was tempted in October of 2020 to buy Bitcoin, but I talked myself out of it, because I truly don't understand it. And the other reason, I couldn't even buy a cup of coffee with it back then. So cryptocurrency to me has no intrinsic value.

SPACs (Special Purpose Acquisition Company aka "blank check companies"): For all intent is a "shell" company used to purchase other companies. These entities raise a bunch of cash from people like you and me with the "founders" of the SPACs generally making a lot of money JUST for putting them together. The intent of the SPAC is to eventually have the company or companies it has purchased to "go public" through an Initial Public Offering. At this point, the "founders" are hopeful everyone will make a bunch of money (greed). From 2013 to 2019, approximately $43 billon was raised in SPACs but in the last 15 months, over $170 billion has been invested in SPACs.

If you've been around long enough, you might remember "Limited Partnerships." These were formed by General Partners (Founders) who raised millions of dollars from investors (limited partners, LPs). The General Partners (founders) made a lot of money from "managing" the assets and raising money. If you are like me, I don't actually know anybody personally or professionally that actually made money investing in LPs other than the General Partners (founders). In fact, my experience along with many others was losing money through LPs, not making money. And to this day, LPs continues to be one of my single worse investment regrets.

So, if you think SPACs are fun, now let us discuss NFTs: An NFT is a Non-Fungible Token, which is a unit of data on a digital ledger called the blockchain. Basically, an NFT is simply a digital item like an image, video, video game, audio file or any other creative work that is digitally stored in a way that ensures the purchaser owns the original. Non-fungible simply means "one-of-a-kind, original, irreplaceable." In the last few months, we've seen just about anything including a single red pixel for $900,000.

Skeptics (like me) of NFTs say most of these will be worthless. Perhaps this will yet be another "bubble" that will be examined in Universities in years to come. But, if you're interested, I have a bunch of participation trophies and awards that I have collected over the years. Rather than simply throw them away, if you are interested, I can digitize the awards and provide you with the original code. My minimum bid is $1m. Or, if you would like to take it from my garage for free to clear space, I'll take that too.

Lastly, Game Stop. While this is old news now, according to Yahoo Finance, Game Stop, symbol GME, was trading around $4 a share in January 2021 only to peak at $347 a share in February 2021. A true lottery wins for those that bough at $4 and sold at $347 and a true lottery waste of money for those who bought at $347 (maybe too early to feel sorry for them as the story is still playing out). How did this happen? Nobody really knows for sure, but the speculation is with the help of social media, it appears the stock price could have escalated in value due to comments that were posted during a social media frenzy. Fortunately, I was not "friends" with anyone in this discussion group, so therefore, I missed it.

In the old days (the 80s and 90s), it was called "manipulation." But due to the formation of social media, the regulators even appear to have no idea how to handle this situation. In the 80s and 90s it was a "boiler room" full of "brokers" that "dialed for dollars" to unknowing investors to put money in "worthless" stocks only to inflate the prices so that the brokers themselves that owned these stocks could sell them at absurdly higher prices. In my finance classes this was known as "pump and dump" which was simply illegal back then.

The one common denominator that all of these have in common (in my opinion) and why people are investing in this way is what we professionally refer to as **FOMO: the Fear of Missing Out**. I know there is more research being done to support each of these speculative investments. But the people I talk to that own each or one of these have one thing in common, their desire is to not miss out, even when they are unable to provide a good reason (my opinion) to get in. The predominant argument is that in their opinion, each or one of them is going to make them "filthy rich" (greed).

Here's the good news. All of us at KFM believe you should not gamble in SPACs, NFTs, Cryptocurrencies or Game Stop. If you want to, it should be done with lottery money mentality.

What hasn't changed in 34 years is "how" people create their own financial success. The number one reason from our perspective comes uniquely from their ability to spend less than what they make. With the difference, they invested in their retirement accounts, or regular investment accounts, or their businesses. They also understood the earlier they started, the less money they would need to set aside because they understood the value of investing for the long-term. In my 34 years of being a financial advisor I am yet to have met anyone that came to financial independence and security through gambling. It has traditionally come from a more moderate way of life, that translates closer to the classic story of the tortoise and the hare. And from what I've witnessed to date, the tortoise always wins.

I apologize for the length of this update. But we wanted to put this out there for discussion during our upcoming meetings. As always, we look forward to connecting in the upcoming days and weeks whether it be virtual or in-person. Should you have any questions or concerns, please reach out to your Team at KFM. Stay safe, healthy and connected. We will see you soon!