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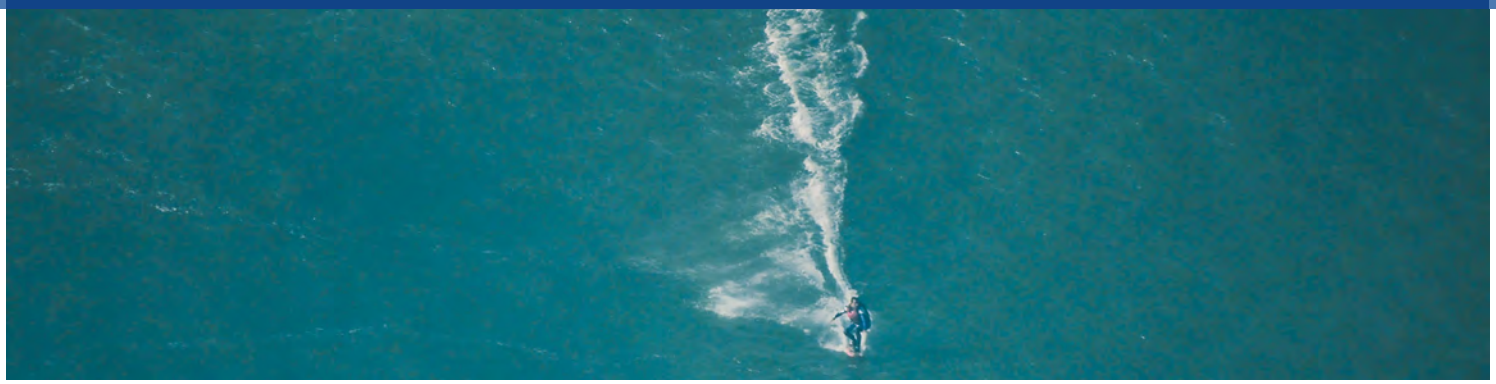

Michel Perera,
Chief Investment Officer

Bitcoin – valid investment or criminally insane?

At a post office, a young woman buying cryptocurrency from a machine was asked why. Her answer was "It's the investment of the future." Really?

Bitcoin is the best known of the 1,800-odd cryptocurrencies. Their meteoric rise has drawn many investors, with some believing that the underlying blockchain technology (blockchain is a digital ledger in which transactions made in cryptocurrencies are recorded chronologically and publicly) could become one of the most powerful tools ever given to civilisation. But do investors understand the risks and does the underlying technology even matter?

What constitutes a suitable investment?

In this discussion, we use bitcoin as proxy for all cryptocurrencies (ethereum, ripple, litecoin, etc.).

To us, any suitable investment requires a valuation methodology, safe custody and easy transferability. Bitcoin fails to meet these tests.

1. **Valuation:** bitcoin has no proper valuation method or underlying value. This is unlike equities which can be valued by their earnings or cash flow, bonds by yield, property by rental income and location and commodities by their industrial usage. There may be scarcity, because only a limited number of bitcoins is produced, but scarcity does not create value unless the product has an economic purpose. Should bitcoin be worth US$10,000, US$100, US$1m or 10 cents? There is no measurement to help you make that decision.
2. **Safety:** other investments have custodians, registries, etc. to protect investors. With bitcoin there is no central financial or other authority such as a bank or government. One astonishing statistic is that so far, 14% of bitcoin has been stolen or lost. The private keys and digital wallets are inherently vulnerable and intermediaries charge enormous amounts to deal with that basic safety issue.
3. **Transferability:** it takes a long time and huge efforts to buy or sell (particularly to sell) bitcoin. 'Mining' – where bitcoin transactions are digitally verified and added to the public 'blockchain' ledger – is highly time-consuming, whereas equities and bonds can be sold in a fraction of a second.

How can we help?

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To top it all, many governments, including South Korea, China and France, are now clamping down on cryptocurrencies. Bank of England Governor Mark Carney warned about a regulatory crackdown. The list will get longer. No wonder: a high percentage of bitcoin is in the hands of criminals, money launderers, malware producers and rogue governments.

Indeed, in an effort to stabilise its economic crisis, Venezuela is issuing its own national cryptocurrency, the petro, in an ICO (initial coin offering – there is one ICO a week these days). It is claimed to be backed by the country's oil, despite the country no longer producing or selling its oil effectively.

Finally, although cryptocurrencies seem to move up and down with risk appetite, their price graphs make the 17th-century tulip craze look like a triple-A rated government bond. More importantly, out of 1,800 outstanding cryptos plus any future ICOs, are you confident you could pick the survivor?

Blockchain may well be one of the technologies of the future (although it scores poorly environmentally, given the huge electricity consumption required for 'mining') but this alone doesn't warrant investing in crypto and there are countless other reasons not to.

How can we help?

If you'd like to talk to us about any of the topics or issues discussed in this article, please contact your Wealth Manager, email us at **marketing@canaccord.com** or call one of the numbers shown below.

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