Opinion **Bitcoin**

Nouriel Roubini: bitcoin is not a hedge against tail risk

Elon Musk may be buying it, but that doesn't mean everyone else should follow suit

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Nouriel Roubini © Joe Buglewicz/Bloomberg

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Claims that bitcoin is the new "digital gold" are feeding a new bubble in it and other cryptocurrencies. The last one in 2017-18 saw bitcoin go from $1,000 to $20,000 and then fall back to $3,000 by the end of 2018.

Since the fundamental value of bitcoin is zero and would be negative if a proper carbon tax was applied to its massive polluting energy-hogging production, I predict that the current bubble will eventually end in another bust.

Referring to bitcoin or other crypto as "currencies" is a misnomer. They are not a unit of account: virtually nothing is priced in them. They are not a scalable means of payment: with bitcoin you can do five transactions per second while the Visa network does 24,000. Bitcoins are barely used by legitimate companies as payment for goods and services, although Tesla said it planned to start accepting them.

Crypto is not a stable store of value: even some crypto conferences refuse to accept them as payment for attendance fees. The volatile price moves can wipe out any profit margin of a merchant within a matter of hours. They aren't even denominated in a consistent way that allows users to compare relative prices of goods. This reliance on different tokens is effectively a return to barter. The Flintstones had a more sophisticated monetary system based on a benchmark: the cartoon cavemen used shells.

Even referring to crypto as assets is a misnomer. Most assets have a stream of income (stocks, bonds, commercial real estate) or a use (housing) or some other utility (fiat currency provides liquidity and can be used for payments). Gold has no income but it has industrial uses. It also has utility as a store of value and a hedge against inflation, currency debasement and tail risks.

Crypto has no income, no utility, no payment or other services. It isn't even anonymous because the underlying blockchain technology makes it easy to trace payments. It is only a play on a speculative asset bubble, worse than tulip-mania as flowers had and still have utility. Its store of value against tail risks is unproven. And worse: some cryptos, dubbed "shitcoins", are financial scams in the first place or debased daily by their sponsor. Bitcoin's price is highly volatile, and claims of misbehaviour, including pump and dump, spoofing, wash trading and front-running by exchanges, are widespread.

Stablecoins claim to be superior. But New York authorities are already investigating whether one, tether, is being used to manipulate the price of bitcoin.

Vitalik Buterin, a co-founder of the cryptocurrency ethereum, argues that no crypto can be at the same time scalable, safe and decentralised. Traditional financial systems are scalable and safe: if your credit card or bank account is hacked or stolen, you are made whole. But they are centralised because participants and assets are verified by trusted institutions. Right now, crypto is neither scalable nor safe. If your private key is stolen or lost, the assets are gone for good.

It isn't even decentralised. Oligopolistic miners control most bitcoin mining. Many are out of reach of western law enforcement in places such as China, Russia and Belarus, creating a national security nightmare. About 99 per cent of bitcoin trading occurs on centralised exchanges, which may be hackable. Furthermore, the original programmers retain outsized control over their creations. In some cases they act as police, prosecutors and judges, and reverse transactions that are supposed to be immutable. Nor is crypto equitable: a small number of "whales" control much of bitcoin's value.

This undermines claims that crypto will decentralise finance, provide banking services to the unbanked, or make the poor rich. Blockchain claims to enable cheap money transfers to refugees, but crypto is much more likely to provide cover for scam artists, conmen, tax evaders, criminals, terrorists and human traffickers.

Our world is beset by financial crises, geopolitical risks and very loose monetary policy. There is growing demand for safe haven assets that are a hedge against inflation, currency depreciation and debasement and tail risks. Gold, inflation-indexed bonds, commodities, real estate and even equities are all reasonable candidates.

Risky, volatile bitcoin doesn't belong in the portfolios of serious institutional investors. Many of its retail backers are suckers being manipulated by an army of self-serving insiders and snake oil salesmen. Tesla's Elon Musk and MicroStrategy's Michael Saylor may be betting the house on bitcoin. That doesn't mean you should.

Letter in response to this article:

Bitcoin's volatility is just growing pains / *From David Crook, Chief Executive, Tail Wind Advisory & Management, London WC2, UK*