

---

# “ONE SMALL STEP FOR MANAGERS, ONE GIANT LEAP FOR BITCOIN” – ON THE EDGE OF A PARADIGM SHIFT

Wisdomtree EU  
30 Mar 2021

Mainstream adoption of technology occurs when a system is robust and its value is recognized by the public. To quantify these measures, let's talk about utility value and speculative value.

**Utility value** refers to the benefits that the technology provides, reflected by its demands.

**Speculative value** is when investors believe the technology is worth.

Both factors are essential in advancing a system's expansion – utility value is unsubstantiated if the speculative value doesn't grow. Reverseely, speculative value is artificial if utility value doesn't follow.

Bitcoin's recent growth is fueled by both aspects. Its ecosystem has matured, leading to more applications in real life. In anticipation of its wider adoption, financial institutions started delving into the crypto space, resulting in a strong inflow of capital.

Unlike its 2017 retail frenzy, Bitcoin's recent upsurge is partly driven by financial institutions' interests.

In our first blog of the series, we introduced corporations' purchases of Bitcoin as part of their balance sheet assets. Here, we will discuss the second source of institutional demand – the investment management industry's participation.

## A Shift in Narrative and Perception

Financial institutions' view of Bitcoin has been evolving.

In the beginning, Bitcoin was mainly regarded as electronic cash, and many saw it as a means to facilitate illicit activities. As time passed, analysis by blockchain analytics companies like Chainalysis have helped debunk the idea that Bitcoin is mostly used for illicit activities – the estimated amount of laundered money accounts for 2-5% of global GDP (\$800B - \$2T), while total illicit value including money laundering related to cryptocurrency accounts for 0.34% (\$10B) of its transaction volume.<sup>1</sup>

The narrative also shifted to acknowledge Bitcoin as a financial asset for a potential store of value, largely per virtue of its limited supply, as well as a good candidate for portfolio diversification.

The current inflationary and low-yield environment aids the financial asset narrative,

as fiat money and bonds become poor vehicles to store value. Furthermore, payment companies' plan to accept Bitcoin and blockchain technology's applications demonstrate one aspect of Bitcoin's utility value. Bitcoin's growing influence has boosted end clients' interests to capture the potential upside of this new technology. Their interests have in turn encouraged asset managers to incorporate it into portfolios.

### The Bitcoin Ecosystem Evolution

Structurally, the underlying Bitcoin network has matured since its birth. The fact that Bitcoin has been in place for more than a decade is a testimony of its operational validity.

Not only are mining machines used today much more advanced, but miners and users also expanded significantly: there are now more than 76K mining nodes and 1.2M active Bitcoin addresses.<sup>2</sup>

The evolution of Bitcoin can also be seen through the development of its trading infrastructure. Trading volumes on the eight major exchanges have passed \$11B, reaching an all-time high.<sup>3</sup> Compared to the early days when Bitcoin first started trading, the current infrastructure offers better custody solutions, more efficient pricing, higher liquidity, and easier access.

- **Better Custody** – When someone “owns” Bitcoins, what they really own are the private keys associated with their Bitcoin wallets. In the past, investors either self-custodied or stored their keys in exchanges' hot wallets. These methods led to regrettable password losses and high-profile hacks. Firms have stepped in with custody solutions to provide safer and more convenient options to protect bitcoin ownership. They generally achieve this by storing private keys (or key fragments) offline – commonly referred to as cold storage. Other technologies, such as multi-party computation (MPC), have also enabled secure key storage.
- **More Efficient Pricing and Higher Liquidity** – Market makers such as DRW's Cumberland, Jane Street, Jump Trading, and Flow Traders got into the crypto space as early as 2014. They provide liquidity, minimize slippage, and reconcile prices across platforms by arbitraging the difference away. Their involvement creates a more efficient market to execute trades.
- **Easier Access** – Institutional investors now have more tools to obtain Bitcoin exposure. Bitcoin futures have grown significantly over the years. We are also witnessing the expansion of Europe's Bitcoin exchange traded fund (ETP) market, as well as the birth of North America's Bitcoin exchange traded fund (ETF) market. Moreover, exchanges such as Coinbase and Gemini are building trading systems that resemble equity systems to bring traditional securities experience to the crypto world.

Bitcoin's network expansion has eased institutional investors' concerns about legitimacy. The development in Bitcoin's trading infrastructure has paved the way for institutional investors' entrance.

### How can investors get access to bitcoin?

Investment managers, either directly or through their affiliates, are taking steps to provide Bitcoin exposure to end clients. Some of the measures include establishing crypto trading operations, offering custody services, financing transactions, and allocating to Bitcoin in their investment funds.

They seek exposure to Bitcoin through the following means:

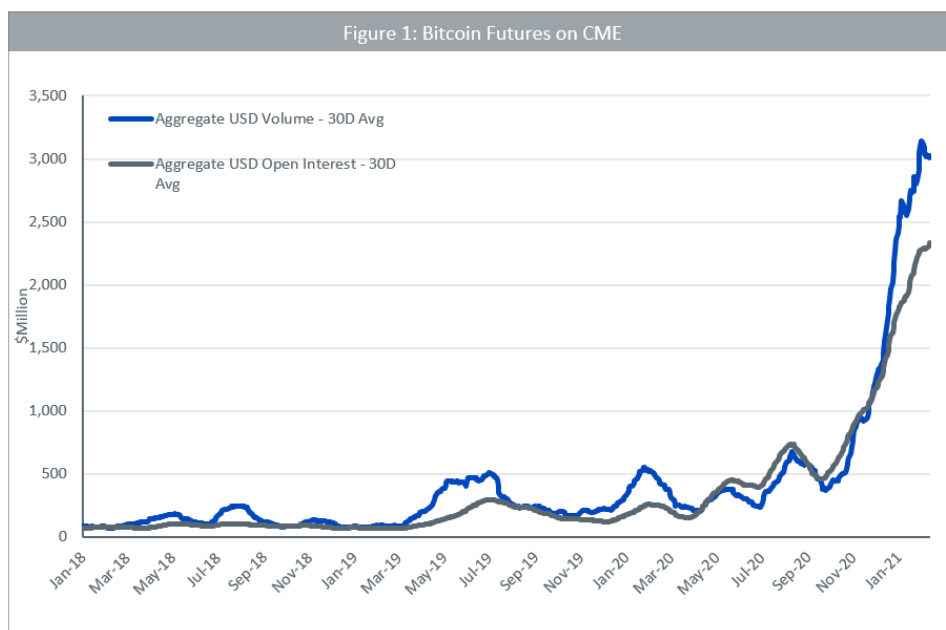
- Direct physical holding of Bitcoins, often through custodians.
- Investment through Bitcoin eETPs/ETFs, which eliminates the burden of managing keys and custody for the investor while providing physical exposure.
- Synthetic exposure through regulated futures like the CME instrument, offering the usual advantages that come with any other commodity futures contract (settlement, ease of shorting, leverage, etc).
- Indirect investment through equities, such as cryptocurrency mining companies or companies that hold bitcoin in their corporate treasury.

### Institutional Money Entering the Futures Market

Regulated Bitcoin futures debuted in December 2017 on the Chicago Mercantile Exchange (CME). Since then, a lot of new buyers have been entering the market via futures. They include family offices, asset managers, and hedge funds.

Because most participants from this channel adhere to strict compliance rules and are prohibited in trading unregulated futures on retail platforms, Bitcoin futures’ open interests and volume on regulated exchanges are important indicators of institutional activities.

Recently, we have witnessed a strong pickup in institutional demand, reflected by significant rises in open interest (over \$2B) and trading volume (close to \$2.8B) on the CME Bitcoin futures.



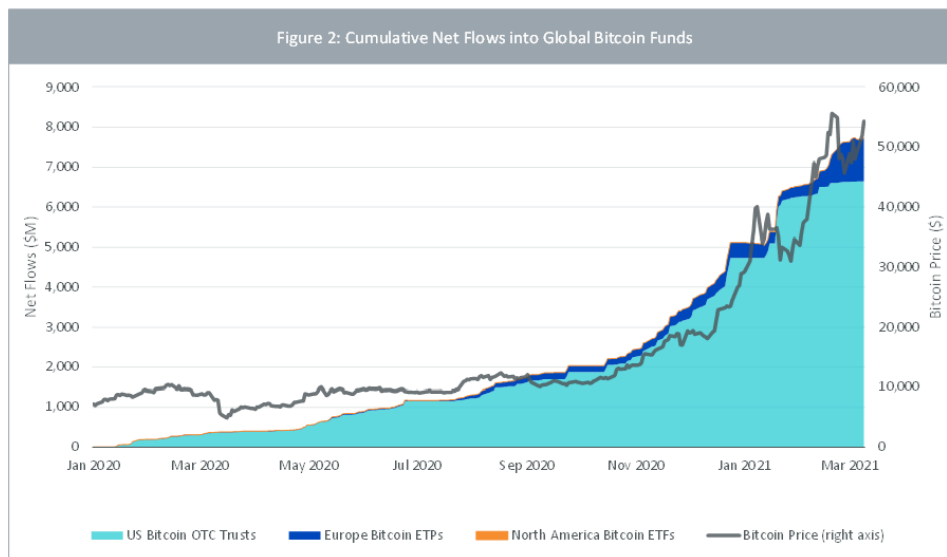
Source: WisdomTree, Bloomberg, from 12/18/2017 to 3/9/2021.

**Historical performance is not an indication of future performance and any investments may go down in value.**

**Bitcoin Trusts and ETPs Bringing Strong Inflows**

Bitcoin trusts, private funds, and ETPs have also taken in significant money in recent months. Since January 2020, Bitcoin ETPs took in nearly \$900M inflows.

The flow has been dominated by European products, and the North American funds are on the rise with the recent launch of Canadian ETFs. OTC-traded trusts, which are currently trading in the US and have existed for a longer period of time, have taken in an even greater sum of money.



Source: WisdomTree, Bloomberg, from 1/1/2020 to 3/9/2021.

**Historical performance is not an indication of future performance and any investments may go down in value.**

In February 2021, Bitcoin ETFs gained regulatory approval in Canada and began trading on the Toronto Stock Exchange. In just one month, the combined AUMs of such ETFs rose to more than \$580M USD. Other jurisdictions, including the US, may follow by allowing bitcoin-focused ETFs and/or allocating greater exposure to bitcoin futures in US registered ETFs.

As we’ve discussed in other blogs, we believe ETPs and ETFs can provide effective access to Bitcoin for investors. The flows into these vehicles indicate continued retail and institutional interests in the asset class.

**Conclusion**

It is important to recognize that Bitcoin’s ecosystem is not yet fully developed, but it is equally important to acknowledge that its landscape is changing rapidly.

As Bitcoin grows organically and realizes its utility value, we believe its speculative value will be gradually substantiated. At this moment, we are witnessing the beginning of a new paradigm, shifting away from a quasi-exclusive retail asset to a more widely

accepted financial instrument.

#### Source

<sup>1</sup> <https://www.unodc.org/unodc/en/money-laundering/overview.html>, Chainalysis 2021 Crypto Crime Report.

<sup>2</sup> <https://www.coindesk.com/are-you-running-a-bitcoin-node>, Glassnode, as of 1/29/2021.

<sup>3</sup> The eight exchanges refer to Bitfinex, Coinbase, Kraken, Bitstamp, bitFlyer, Gemini, itBit, Poloniex. <https://www.coindesk.com/bitcoin-active-addresses-trading-volumes-all-time-highs>

#### Related blogs

+ [Bitcoin' s Growing Demands Part 1: Balance Sheets to the Moon](#)

+ [Bitcoin and the Planet](#)

#### Related products

+ [Wisdomtree Bitcoin](#)

View the online version of this article [here](#).

Important Information

**Marketing communications issued in the European Economic Area (“EEA”):** This document has been issued and approved by WisdomTree Ireland Limited, which is authorised and regulated by the Central Bank of Ireland.

**Marketing communications issued in jurisdictions outside of the EEA:** This document has been issued and approved by WisdomTree UK Limited, which is authorised and regulated by the United Kingdom Financial Conduct Authority.

WisdomTree Ireland Limited and WisdomTree UK Limited are each referred to as “WisdomTree” (as applicable). Our Conflicts of Interest Policy and Inventory are available on request.

**For professional clients only.** The information contained in this document is for your general information only and is neither an offer for sale nor a solicitation of an offer to buy securities or shares. This document should not be used as the basis for any investment decision. Investments may go up or down in value and you may lose some or all of the amount invested. Past performance is not necessarily a guide to future performance. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

The application of regulations and tax laws can often lead to a number of different interpretations. Any views or opinions expressed in this communication represent the views of WisdomTree and should not be construed as regulatory, tax or legal advice. WisdomTree makes no warranty or representation as to the accuracy of any of the views or opinions expressed in this communication. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice.

This document is not, and under no circumstances is to be construed as, an advertisement or any other step in furtherance of a public offering of shares or securities in the United States or any province or territory thereof. Neither this document nor any copy hereof should be taken, transmitted or distributed (directly or indirectly) into the United States.

Although WisdomTree endeavours to ensure the accuracy of the content in this document, WisdomTree does not warrant or guarantee its accuracy or correctness. Where WisdomTree has expressed its own opinions related to product or market activity, these views may change. Neither WisdomTree, nor any affiliate, nor any of their respective officers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this document or its contents.