



Has the Bitcoin Bubble Burst?

Description

Bitcoin's latest sharp decline in value sees it trading at less than half of its 2017 peak of US\$19,343. That has caused the **Bitcoin Investment Trust** (NASDAQOTH:GBTC) to plummet by a massive 36% for the year to date, and there is every sign that it is headed lower.

Clearly, such a momentous decline in value has caused many investors to lose significant amounts of money with no sign that it can be recovered. While the Bitcoin fans continue to talk up the prospects of it and other cryptocurrencies, there is every sign that they are headed to zero, which will be a tremendous blow for cryptocurrencies and related companies.

Now what?

The fundamental problem with Bitcoin is that it can't be valued. Its value is solely extrinsic, which means that it is determined by how much demand there is for the digital currency rather than by any underlying fundamental factors such as sales, earnings, or cash flow.

One fundamental factor which many fans fail to acknowledge is that Bitcoin has yet to be widely adopted as a currency, meaning that it is even failing to meet its original intent. The likelihood of it ever becoming a generally accepted means of exchange is slim, as transaction processing times and costs keep rising.

For these reasons, Bitcoin's value is subject to whims of investors and market sentiment, hence the incredible volatility witnessed in recent months.

From the start of 2017 to mid-December, its price rose about 19-fold.

In fact, its price exploded, as it adopted all the characteristics of a [traditional market bubble](#). These included a parabolic price curve, the following of messianic fans, and claims of a new paradigm where traditional asset-valuation methodologies didn't apply.

There was considerable concern from regulators, finance industry bodies, and government representatives, as less sophisticated investors piled in cryptocurrencies at a frantic rate, in many

cases using credit to fund their investments. That has seen a [push for regulation](#), as governments and regulators seek to protect investors from volatile investments that are difficult to understand and almost impossible to value.

Nonetheless, Bitcoin's latest recovery, which sees it up by almost 40% since bottoming at just under US\$6,000 on February 6, appears to be nothing more than a "dead cat bounce"; believers claim there is a return to normal. Once this recovery is over, there is every sign that Bitcoin could plummet yet again, falling to new lows as it enters the "blow-off phase."

So what?

The risks this poses to investors in the Bitcoin Investment Trust are tremendous. As an over-the-counter stock, it is highly illiquid and difficult to exit, and it is trading at a considerable premium to the value of the Bitcoin that it holds. If we look at the numbers the Trust based the value of the Bitcoin that it holds, and the number of shares outstanding, it should be trading at ~US\$8.37 per share. Instead, its market price at the time of writing is US\$14.25 per share, which represents a 70% premium. That leaves it vulnerable to any further decline in the value of Bitcoin.

The same can be seen with cryptocurrency stocks such as **HIVE Blockchain Technologies Ltd.** ([TSXV:HIVE](#)), which has yet to report a profit. Its stock soared by over 400% between September 2017 and early November; since then it has pulled back sharply to be trading at less than half of its November peak. Should cryptocurrencies fail, it would cause HIVE's stock to plunge, potentially leaving it worthless.

Bitcoin's significant drop in value should serve as a reminder to investors that investing for the long term in easily understood investments should be their priority rather than dabbling in the latest hot investment, no matter how appealing it may be.

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